

EXTREME NETWORKS INC  
Form 10-Q  
May 07, 2015  
Table of Contents

---

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D. C. 20549

---

Form 10-Q

---

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2015

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 000-25711

EXTREME NETWORKS, INC.  
(Exact name of registrant as specified in its charter)

DELAWARE  
[State or other jurisdiction  
of incorporation or organization]

77-0430270  
[I.R.S Employer  
Identification No.]

145 Rio Robles,  
San Jose, California  
[Address of principal executive office]

95134  
[Zip Code]

Registrant's telephone number, including area code: (408) 579-2800

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Edgar Filing: EXTREME NETWORKS INC - Form 10-Q

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

The number of shares of the Registrant's Common Stock, \$.001 par value, outstanding at April 29, 2015 was 100,053,435.

---

Table of Contents

EXTREME NETWORKS, INC.  
 FORM 10-Q  
 QUARTERLY PERIOD ENDED March 31, 2015  
 INDEX

	PAGE
<u>PART I. CONDENSED CONSOLIDATED FINANCIAL INFORMATION</u>	
Item 1. <u>Condensed Consolidated Financial Statements (Unaudited):</u>	
<u>Condensed Consolidated Balance Sheets as of March 31, 2015 and June 30, 2014</u>	<u>3</u>
<u>Condensed Consolidated Statements of Operations for the Three and Nine Months ended March 31, 2015 and March 31, 2014</u>	<u>4</u>
<u>Condensed Consolidated Statements of Comprehensive Loss for the Three and Nine Months ended March 31, 2015 and March 31, 2014</u>	<u>5</u>
<u>Condensed Consolidated Statements of Cash Flows for the Nine Months ended March 31, 2015 and March 31, 2014</u>	<u>6</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>7</u>
Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>20</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>28</u>
Item 4. <u>Controls and Procedures</u>	<u>30</u>
<u>PART II. OTHER INFORMATION</u>	
Item 1. <u>Legal Proceedings</u>	<u>31</u>
Item 1A <u>Risk Factors</u>	<u>31</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>43</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>43</u>
Item 4. <u>Mine Safety Disclosure</u>	<u>43</u>
Item 5. <u>Other Information</u>	<u>43</u>
Item 6. <u>Exhibits</u>	<u>44</u>
<u>Signatures</u>	<u>45</u>



Table of Contents

EXTREME NETWORKS, INC.  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (In thousands, except share and per share amounts)  
 (Unaudited)

	March 31, 2015	June 30, 2014
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$74,067	\$73,190
Short-term investments	1,506	32,692
Accounts receivable, net of allowances of \$4,344 at March 31, 2015 and \$3,618 at June 30, 2014	78,727	124,664
Inventories	66,811	57,109
Deferred income taxes	797	1,058
Prepaid expenses and other current assets	10,069	14,143
Total current assets	231,977	302,856
Property and equipment, net	42,399	46,554
Intangible assets, net	61,096	87,459
Goodwill	70,877	70,877
Other assets	25,029	18,686
Total assets	\$431,378	\$526,432
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$9,750	\$29,688
Accounts payable	46,378	37,308
Accrued compensation and benefits	20,502	26,677
Accrued warranty	7,879	7,551
Deferred revenue, net	73,206	74,735
Deferred distributors revenue, net of cost of sales to distributors	35,687	31,992
Other accrued liabilities	29,820	38,357
Total current liabilities	223,222	246,308
Deferred revenue, less current portion	23,141	22,942
Long-term debt, less current portion	58,750	91,875
Deferred income taxes	2,572	—
Other long-term liabilities	7,934	8,595
Commitments and contingencies (Note 8)		
Stockholders' equity:		
Convertible preferred stock, \$.001 par value, issuable in series, 2,000,000 shares authorized; none issued	—	—
Common stock, \$.001 par value, 750,000,000 shares authorized; 100,050,411 shares issued and outstanding at March 31, 2015 and 96,980,214 shares issued and outstanding at June 30, 2014	100	97
Additional paid-in-capital	861,653	845,267
Accumulated other comprehensive loss	(1,798	) (439 )
Accumulated deficit	(744,196	) (688,213 )
Total stockholders' equity	115,759	156,712
Total liabilities and stockholders' equity	\$431,378	\$526,432
See accompanying notes to condensed consolidated financial statements.		



Table of Contents

EXTREME NETWORKS, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (In thousands, except per share amounts)  
 (Unaudited)

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Net revenues:				
Product	\$86,527	\$109,891	\$301,700	\$290,001
Service	33,063	31,871	101,372	74,260
Total net revenues	119,590	141,762	403,072	364,261
Cost of revenues:				
Product	49,761	58,703	164,282	153,112
Service	12,105	12,204	35,377	26,742
Total cost of revenues	61,866	70,907	199,659	179,854
Gross profit:				
Product	36,766	51,188	137,418	136,889
Service	20,958	19,667	65,995	47,518
Total gross profit	57,724	70,855	203,413	184,407
Operating expenses:				
Research and development	23,858	24,265	71,205	53,098
Sales and marketing	39,226	44,703	127,976	108,033
General and administrative	9,711	11,178	31,091	29,301
Acquisition and integration costs	1,725	6,443	9,283	18,826
Restructuring charge, net of reversals	—	(6	) —	499
Amortization of intangibles	4,467	7,666	13,402	11,444
Total operating expenses	78,987	94,249	252,957	221,201
Operating loss	(21,263	) (23,394	) (49,544	) (36,794
Interest income	129	156	471	603
Interest expense	(758	) (764	) (2,419	) (1,288
Other expense, net	(535	) (146	) (1,033	) (1,338
Loss before income taxes	(22,427	) (24,148	) (52,525	) (38,817
Provision for income taxes	1,121	910	3,458	2,262
Net loss	\$(23,548	) \$(25,058	) \$(55,983	) \$(41,079
Basic and diluted net loss per share:				
Net loss per share – basic	\$(0.24	) \$(0.26	) \$(0.57	) \$(0.43
Net loss per share – diluted	\$(0.24	) \$(0.26	) \$(0.57	) \$(0.43
Shares used in per share calculation – basic	99,783	96,069	98,591	95,116
Shares used in per share calculation – diluted	99,783	96,069	98,591	95,116

See accompanying notes to condensed consolidated financial statements.

Table of Contents

EXTREME NETWORKS, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS  
 (In thousands)  
 (Unaudited)

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Net loss:	\$ (23,548	) \$ (25,058	) \$ (55,983	) \$ (41,079
Other comprehensive income, net of tax:				
Available for sale securities:				
Change in unrealized (losses) gains on available for sale securities, net of taxes	(1	) (95	) (26	) 138
Reclassification of adjustment for realized net gains on available for sale securities included in net loss	—	10	—	158
Net change in unrealized (losses) gains on available for sale securities, net of taxes	(1	) (85	) (26	) 296
Net change in foreign currency translation adjustments	87	48	(1,333	) 1,005
Other comprehensive (loss) income	86	(37	) (1,359	) 1,301
Total comprehensive loss	\$ (23,462	) \$ (25,095	) \$ (57,342	) \$ (39,778

See accompanying notes to condensed consolidated financial statements.



Table of Contents

EXTREME NETWORKS, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (In thousands)  
 (Unaudited)

	Nine Months Ended	
	March 31, 2015	March 31, 2014
Cash flows from operating activities:		
Net loss	\$(55,983 )	\$(41,079 )
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation	9,652	7,767
Amortization of intangible assets	26,977	18,937
Provision for doubtful accounts and allowance for sales returns	4,317	898
Stock-based compensation	13,935	9,874
Other non-cash charges	628	2,267
Changes in operating assets and liabilities, net		
Accounts receivable	41,620	(24,171 )
Inventories	(9,702 )	(13,313 )
Prepaid expenses and other assets	806	(1,354 )
Accounts payable	9,070	(5,404 )
Accrued compensation and benefits	(6,176 )	(1,764 )
Deferred revenue	(1,331 )	10,796
Deferred distributor revenue, net of cost of sales to distributors	3,696	6,829
Other current and long term liabilities	(3,945 )	(900 )
Net cash provided by (used in) operating activities	33,564	(30,617 )
Cash flows from investing activities:		
Capital expenditures	(5,610 )	(17,384 )
Acquisition, net of cash acquired	—	(180,000 )
Purchases of investments	—	(9,045 )
Purchases of non-marketable equity investments	(3,000 )	—
Proceeds from maturities of investments and marketable securities	21,815	26,722
Proceeds from sales of investments and marketable securities	9,051	56,594
Purchases of intangible assets	(569 )	—
Net cash provided by (used in) investing activities	21,687	(123,113 )
Cash flows from financing activities:		
Borrowings under Revolving Facility	24,000	59,000
Issuance of Term Loan	—	65,000
Repayment of debt	(77,062 )	(1,625 )
Proceeds from issuance of common stock	2,455	6,296
Net cash (used in) provided by financing activities	(50,607 )	128,671
Foreign currency effect on cash	(3,767 )	611
Net increase (decrease) in cash and cash equivalents	877	(24,448 )
Cash and cash equivalents at beginning of period	73,190	95,803
Cash and cash equivalents at end of period	\$74,067	\$71,355

See accompanying notes to the condensed consolidated financial statements.

6

---

Table of Contents

EXTREME NETWORKS, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The unaudited condensed consolidated financial statements of Extreme Networks, Inc. (referred to as the “Company” or “Extreme Networks”) included herein have been prepared under the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted under such rules and regulations. The condensed consolidated balance sheet at June 30, 2014 was derived from audited financial statements as of that date but does not include all disclosures required by generally accepted accounting principles for complete financial statements. These interim financial statements and notes should be read in conjunction with the Company’s audited consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended June 30, 2014.

The unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments that, in the opinion of management, are necessary for a fair presentation of the results of operations and cash flows for the interim periods presented and the financial condition of Extreme Networks at March 31, 2015. The results of operations for the three and nine months ended March 31, 2015 are not necessarily indicative of the results that may be expected for fiscal 2015 or any future periods.

2. Summary of Significant Accounting Policies

For a description of significant accounting policies, see Note 3, Summary of Significant Accounting Policies, to the consolidated financial statements included in the Company's Annual report on Form 10-K for the fiscal year ended June 30, 2014. There have been no material changes to the Company's significant accounting policies since the filing of the Annual report on Form 10-K.

3. Recently Issued Accounting Pronouncements

In May 2014, the FASB, jointly with the International Accounting Standards Board, issued Accounting Standard Update No. 2014-09 (Topic 606) - Revenue from Contracts with Customers ("ASU 2014-09"). This ASU's core principle is that a reporting entity will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying this new guidance to contracts within its scope, an entity will: (1) identify the contract(s) with a customer, (2) identify the performance obligation in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation. Additionally, this new guidance will require significantly expanded disclosures about revenue recognition. ASU 2014-09 is effective for annual reporting periods (including interim reporting periods within those annual periods) beginning after December 15, 2016. In April 2015, the FASB approved a one-year deferral of the effective date of the new standard. The new standard will be effective for the Company’s fiscal 2019, with early adoption permitted.

Entities have the option of using either a full retrospective or a modified retrospective approach to adopt this ASU. The Company is currently evaluating the potential effect on its consolidated financial statements from adoption of this standard.

In November 2014, the FASB has issued ASU 2014-15, Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern, which provides guidance on determining when and how to disclose going-concern uncertainties in the financial statements. The new standard requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year of the date of issuance of the entity’s financial statements and provide certain disclosures when there is substantial doubt about the entity’s ability to continue as a going concern. This guidance applies to all entities and is effective for annual periods beginning after December 15, 2015, and interim periods thereafter, with early adoption permitted. The Company is currently evaluating the potential effect on its consolidated financial statements from adoption of this standard.

In January 2015, the FASB issued ASU 2015-01 which provides guidance on the elimination of the concept of extraordinary items under GAAP. This ASU is effective for annual periods ending after December 15, 2016, and interim periods within those fiscal years, with early adoption permitted. The Company is currently evaluating the potential effect on its consolidated financial statements from adoption of this standard.

In February 2015, the FASB issued ASU 2015-02 which provides consolidation guidance and changes the way reporting enterprises evaluate consolidation for limited partnerships, investment companies and similar entities, as well as variable interest

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

entities. The ASU is effective for annual and interim periods in fiscal years beginning after December 15, 2015. The Company is currently evaluating the potential effect on its consolidated financial statements from adoption of this standard.

In April 2015, the FASB issued ASU 2015-03 – Simplifying the Presentation of Debt Issuance Costs, which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 requires retrospective adoption and will be effective for annual and interim periods in fiscal years beginning after December 15, 2015. Early adoption is permitted. The Company is currently evaluating the potential effect on its consolidated financial statements from adoption of this standard.

## 4. Business combinations

On October 31, 2013, (the “Acquisition Date”), the Company completed the acquisition of Enterasys Networks, Inc. (“Enterasys”), a privately held provider of wired and wireless network infrastructure and security solutions, for \$180.0 million, net of cash acquired. The Company also assumed outstanding options and restricted stock units of Enterasys at the Acquisition Date, all of which were unvested.

The acquisition was accounted for using the acquisition method of accounting. The preliminary and final purchase price allocation as of the date of the acquisition is set forth in the table below and reflects various fair value estimates. The following table summarizes the final allocation as of September 30, 2014, of the tangible and identifiable intangible assets acquired and liabilities assumed as compared to the allocation as of December 31, 2013, the quarter in which the transaction was completed (in thousands):

	Preliminary Allocation as of December 31, 2013 (Initial allocation)	Change during the measurement period		Final Allocation as of September 30, 2014	
Cash	\$4,969	\$2,428	a	\$7,397	
Receivables	25,699	(2,428)	) a	23,271	
Inventory	33,662	—		33,662	
Other current assets	8,888	(1,514)	) b	7,374	
Property and equipment	23,122	(1,829)	) c	21,293	
Identifiable intangible assets	108,900	—	d	108,900	
In-process research and development	3,000	—		3,000	
Deferred tax assets	9	—		9	
Other assets	7,343	—		7,343	
Goodwill	57,922	12,955		70,877	
Current liabilities	(75,394)	) (6,141)	) c,e,f	(81,535)	)
Other long-term liabilities	(13,151)	) (1,043)	) c	(14,194)	)
Total purchase price allocation	\$184,969	\$2,428		\$187,397	
Less: Cash acquired from acquisition	(4,969)	) (2,428)	) a	(7,397)	)
Total purchase price consideration, net of cash acquired	\$180,000	\$—		\$180,000	

a. The Company finalized the working capital adjustment as of September 30, 2014, which led to a decrease of \$2.4 million in receivables and a corresponding increase in cash. As a result of this adjustment, the total cash acquired from the acquisition also increased by the same amount. The net effect of this adjustment is an increase in goodwill

of \$2.4 million.

The Company obtained new information regarding the existence of prepaid assets as of the acquisition date which led to a decrease in the fair value of current assets of \$1.5 million, and a corresponding increase in goodwill. The change in the amortization of prepaid assets due to the change in fair value of current assets was immaterial.

The Company updated its preliminary estimate of the fair value of property and equipment which led to a decrease of \$3.0 million in property and equipment with a corresponding increase in goodwill. The Company also updated the fair values of the asset retirement obligations and the related asset retirement assets which led to an increase in the fair value of property and equipment of \$1.2 million and a corresponding increase in current liabilities and other long-term liabilities

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

of \$0.2 million and \$1.0 million, respectively. The decrease in depreciation expense due to the change in fair value of property and equipment was immaterial.

During the nine months ended September 30, 2014, there were no changes to the fair value of the identifiable d. intangible assets acquired. However, the Company revised the estimated useful life of Order backlog from 1.5 years to 1 year.

The Company obtained new information regarding accruals for litigation and statutory tax assessment as of the e. acquisition date which led to an increase in the fair value of current liabilities of \$5.4 million and a corresponding increase in goodwill.

The Company obtained new information regarding the existence of accrued liabilities as of the acquisition date f. which led to a net increase in the fair value of accrued liabilities by \$0.5 million with a corresponding increase in goodwill.

## 5. Balance Sheet Accounts

Cash, Cash Equivalents, Short-Term Investments

Summary of Cash and Available-for-Sale Securities (in thousands)

	March 31, 2015	June 30, 2014
Cash	\$54,288	\$72,623
Cash equivalents	19,779	567
Short-term investments	1,506	32,692
Total available-for-sale	\$21,285	\$33,259
Total cash, cash equivalents and available-for-sale securities	\$75,573	\$105,882

Available-for-Sale Securities

The following is a summary of available-for-sale securities (in thousands):

	Amortized Cost	Fair Value	Unrealized Holding Gains	Unrealized Holding Losses
March 31, 2015				
Money market funds	\$19,779	\$19,779	\$—	\$—
U.S. corporate debt securities	1,506	1,506	—	—
	\$21,285	\$21,285	\$—	\$—
Classified as:				
Cash equivalents	\$19,779	\$19,779	\$—	\$—
Short-term investments	1,506	1,506	—	—
	\$21,285	\$21,285	\$—	\$—
June 30, 2014				
Money market funds	\$567	\$567	\$—	\$—
U.S. corporate debt securities	32,578	32,692	114	—
	\$33,145	\$33,259	\$114	\$—
Classified as:				
Cash equivalents	\$567	\$567	\$—	\$—
Short-term investments	32,578	32,692	114	—
	\$33,145	\$33,259	\$114	\$—





Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The amortized cost and estimated fair value of available-for-sale investments in debt securities at March 31, 2015, by contractual maturity, were as follows (in thousands):

	Amortized Cost	Fair Value
Due in 1 year or less	\$21,285	\$21,285
Total investments in available-for-sale debt securities	\$21,285	\$21,285

The Company considers highly liquid investments with maturities of three months or less at the date of purchase to be cash equivalents. Investments with original maturities of greater than three months, but less than one year at the balance sheet date are classified as Short-term investments.

The Company accumulates unrealized gains and losses on the Company's available-for-sale debt securities, net of tax, in accumulated other comprehensive income (loss) in the stockholders' equity section of its balance sheets. If the fair value of an available-for-sale debt instrument is less than its amortized cost basis, an other-than-temporary impairment is triggered in circumstances where (1) the Company intends to sell the instrument, (2) it is more likely than not that the Company will be required to sell the instrument before recovery of its amortized cost basis, or (3) the Company does not expect to recover the entire amortized cost basis of the instrument (that is, a credit loss exists).

The Company determines the basis of the cost of a security sold or the amount reclassified out of accumulated other comprehensive income (loss) into earnings using the specific identification method. The Company recorded an other-than temporary impairment loss of \$148,000 during the nine months ended March 31, 2014.

Deferred Revenue, Net

Deferred revenue, net represents amounts for (i) deferred services revenue (support arrangements, professional services and training), and (ii) deferred product revenue net of the related cost of revenue when the revenue recognition criteria have not been met. The following table summarizes deferred revenue, net (in thousands):

	March 31, 2015	June 30, 2014
Deferred services	\$88,737	\$89,657
Deferred product and other revenue	7,610	8,020
Total deferred revenue	96,347	97,677
Less: current portion	73,206	74,735
Non-current deferred revenue, net	\$23,141	\$22,942

The Company offers for sale to its customers, renewable support arrangements that range from one to five years. Deferred support revenue is included within deferred revenue, net within the services category above. The change in the Company's deferred support revenue balance in relation to these arrangements was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Balance beginning of period	\$91,373	\$81,485	\$89,657	\$38,003
Assumed from acquisition	—	—	—	35,879
New support arrangements	27,198	30,986	91,254	77,475
Recognition of support revenue	(29,834	) (28,265	) (92,174	) (67,151
Balance end of period	88,737	84,206	88,737	84,206

Edgar Filing: EXTREME NETWORKS INC - Form 10-Q

Less: current portion	65,596	64,539	65,596	64,539
Non-current deferred revenue	\$23,141	\$19,667	\$23,141	\$19,667

Deferred Distributors Revenue, Net of Cost of Sales to Distributors

The Company records revenue from its distributors on a sell-through basis, recording deferred revenue and deferred cost of sales associated with all sales transactions to its distributors in "Deferred distributor' revenue, net of cost of sales to distributors"

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

in the liability section of its condensed consolidated balance sheet. The amount shown as “Deferred distributors revenue, net of cost of sales to distributors” represents the deferred gross profit on sales to distributors based on contractual pricing.

The following table summarizes deferred distributors revenue, net of cost of sales to distributors (in thousands):

	March 31, 2015	June 30, 2014
Deferred distributors' revenue	\$46,230	\$40,715
Deferred cost of sales to distributors	(10,543	) (8,723
Deferred distributors revenue, net of cost of sales to distributors	\$35,687	\$31,992

**Debt**

The Company's debt is comprised of the following (in thousands):

	March 31, 2015	June 30, 2014
Current portion of long-term debt:		
Term Loan	\$9,750	\$5,688
Revolving Facility	—	24,000
Current portion of long-term debt	\$9,750	\$29,688
Long-term debt, less current portion:		
Term Loan	\$48,750	\$56,875
Revolving Facility	10,000	35,000
Total long-term debt, less current portion	58,750	91,875
Total debt	\$68,500	\$121,563

On October 31, 2013, the Company entered into a Credit Agreement (the “Credit Agreement”) which provides for a five-year revolving credit facility for up to \$60.0 million (the “Revolving Facility”) and a \$65.0 million five-year term loan (the “Term Loan”) and together with the Revolving Facility (the “Senior Secured Credit Facilities”). The Company drew \$24.0 million in the first quarter of fiscal 2015 to fund working capital requirements. During the three months ended December 31, 2014, the Company amended the Credit Agreement and among other things modified certain financial covenants governing quick and leverage ratios. The Company repaid \$30.0 million and \$19.0 million of the Revolving Facility during the second and third fiscal quarters of 2015, respectively.

The Credit Agreement contains, among others, certain financial covenants that require the Company to maintain defined minimum financial ratios which limit the Company’s availability to borrowings under the Revolving Facility. As of March 31, 2015, the Company had \$8.6 million of additional availability under the Revolving Facility, due to these financial covenants.

The Company had \$1.0 million of outstanding letters of credit as of March 31, 2015.

**Guarantees and Product Warranties**

Upon issuance of a standard product warranty, the Company discloses and recognizes a liability for the obligation it assumes under the warranty. The Company’s standard hardware warranty period is typically 12 months from the date of shipment to end-users and 90 days for software. For certain products, the Company offers a limited lifetime hardware warranty commencing on the date of shipment from the Company and ending five (5) years following the Company’s announcement of the end of sale of such product. The following table summarizes the activity related to the Company’s product warranty liability during the three and nine months ended March 31, 2015 and 2014, (in thousands):



Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Balance beginning of period	\$7,845	\$7,479	\$7,551	\$3,296
Assumed from acquisition	—	—	—	3,732
New warranties issued	1,751	1,824	5,699	4,782
Warranty expenditures	(1,717 )	(1,478 )	(5,371 )	(3,985 )
Balance end of period	\$7,879	\$7,825	\$7,879	\$7,825

The Company has agreed to hold the customer harmless against losses arising from a breach of intellectual property infringement or other claims made against certain parties. These agreements may limit the time within which an indemnification claim can be made and the amount of the claim. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is not estimable. We have not recorded a liability related to these indemnification and guarantee provisions and our guarantee and indemnification arrangements have not had any significant impact on our consolidated financial statements to date.

**Concentrations**

The Company may be subject to concentration of credit risk as a result of certain financial instruments consisting principally of marketable investments and accounts receivable. The Company has placed its investments with high-credit quality issuers. The Company does not invest an amount exceeding 10% of its combined cash, cash equivalents, short-term investments and marketable securities in the securities of any one obligor or maker, except for obligations of the United States government, obligations of United States government agencies and money market accounts.

The following table sets forth major customers accounting for 10% or more of our net revenue for the periods indicated:

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Westcon Group, Inc.	16%	14%	14%	13%
ScanSource, Inc.	13%	*	*	*
Tech Data Corporation	*	16%	14%	12%

\* Less than 10% of net revenue

**6. Fair Value Measurements**

A three-tier fair value hierarchy is utilized to prioritize the inputs used in measuring fair value. The hierarchy gives the highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels are defined as follows:

Level 1 Inputs - unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 Inputs - quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument; and

Level 3 Inputs - unobservable inputs reflecting the Company's own assumptions in measuring the asset or liability at fair value.

The Company uses forward foreign currency contracts to hedge market risks relating to possible adverse changes in foreign exchange rates.

12

---

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table presents the Company's fair value hierarchy for its financial assets measured at fair value on a recurring basis (in thousands):

March 31, 2015	Level 1	Level 2	Level 3	Total
Assets				
Investments:				
Money market funds	\$ 19,779	\$—	\$—	\$ 19,779
Corporate notes/bonds	—	1,506	—	1,506
Non-marketable equity investment	—	—	3,000	3,000
Total	\$ 19,779	\$ 1,506	\$ 3,000	\$ 24,285
June 30, 2014	Level 1	Level 2	Level 3	Total
Assets				
Investments:				
Money market funds	\$ 567	\$—	\$—	\$ 567
Corporate notes/bonds	—	32,692	—	32,692
Foreign currency forward contracts	—	21	—	21
Total	\$ 567	\$ 32,713	\$—	\$ 33,280

Level 2 investment valuations are based on inputs such as quoted market prices of similar instruments, dealer quotations or valuations provided by alternative pricing sources supported by observable inputs. These generally include U.S. government and sovereign obligations, most government agency securities, investment-grade corporate bonds, and state, municipal and provincial obligations. There were no transfers of assets or liabilities between Level 1 and Level 2 during the three and nine months ended March 31, 2015.

During the quarter, the Company obtained a \$3.0 million equity interest in a Company that operates in the enterprise software platform industry. The Company has not entered into any other transactions with the entity that are considered significant to the Company's consolidated financial statements during the three and nine months ended March 31, 2015.

The Company reflects a non-marketable equity investment as Level 3 in the fair value hierarchy as it is based on unobservable inputs that market participants would use in pricing this asset due to the absence of recent comparable market transactions and inherent lack of liquidity. Significant inputs and assumptions are management's estimate of the enterprise value used to calculate the present value of the asset. Significant changes in any Level 3 input or assumption would result in increases or decreases to fair value measurements for this asset.

There were no liabilities as of March 31, 2015 that were being measured using fair value on a recurring basis. The fair values of accounts receivable, accounts payable, and accrued liabilities, due within one year approximates their carrying values due to their short-term nature.

The Company does not have any assets or liabilities measured at fair value on a non-recurring basis as of March 31, 2015, and June 30, 2014.

## 7. Share-based Compensation

As of March 31, 2015, the Company had 15,578,378 shares available for issuance, of which 12,000,000 shares are available under the 2014 Employee Stock Purchase Plan ("ESPP"), which was approved by the shareholders on November 12, 2014. There are 66,382 shares available under the 1999 ESPP and 3,511,996 shares available under the 2013 Stock Plan.





Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Share-based compensation expense recognized in the condensed consolidated financial statements by line item caption is as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Cost of product revenue	\$265	\$268	\$823	\$568
Cost of service revenue	254	420	816	623
Research and development	1,423	1,419	4,611	2,559
Sales and marketing	1,291	1,765	4,414	3,614
General and administrative	1,139	970	3,271	2,510
Total share-based compensation expense	\$4,372	\$4,842	\$13,935	\$9,874

The Company did not capitalize any stock-based compensation expense in inventory, as the amounts were immaterial during the three and nine months ended March 31, 2015 and 2014, respectively.

Stock Awards

Stock awards may be granted under the 2013 Plan on terms approved by the Board of Directors. Stock awards generally provide for the issuance of restricted stock which vests over a fixed period.

During the three months ended March 31, 2015, the Company began expensing market-performance based restricted stock units to senior executive officers that had been granted during the second quarter of fiscal 2015.

The following table summarizes stock award activity for the nine months ended March 31, 2015:

	Number of Shares (000's)	Weighted- Average Grant- Date Fair Value	Aggregate Fair Market Value (\$000's)
Non-vested stock outstanding at June 30, 2014	6,000	\$ 4.98	
Granted	1,305	\$ 3.45	
Vested	(2,216 )	\$ 5.09	\$7,985
Cancelled	(409 )	\$ 4.42	
Non-vested stock outstanding at March 31, 2015	4,680	\$ 4.55	

Stock Options

The following table summarizes stock option activity under all plans for the nine months ended March 31, 2015.

	Number of Shares (000's)	Weighted- Average Exercise Price Per Share	Weighted- Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (000's)
Options outstanding at June 30, 2014	11,732	\$4.26	5.13	\$ 6,846
Granted	1,153	\$4.11		
Exercised	(425 )	\$3.17		\$ 381
Cancelled	(1,245 )	\$5.12		
Options outstanding at March 31, 2015	11,215	\$4.19	4.73	\$ 493
Exercisable at March 31, 2015	6,047	\$3.95	3.94	\$ 473

Edgar Filing: EXTREME NETWORKS INC - Form 10-Q

Vested and expected to vest at March 31, 2015	10,441	\$4.17	4.66	\$ 489
---	--------	--------	------	--------

The weighted-average grant-date per share fair value of options granted was \$1.34 and \$2.71 during the three months ended March 31, 2015 and 2014, respectively.

The weighted-average grant-date per share fair value of options granted was \$1.91 and \$2.39 during the nine months ended March 31, 2015 and 2014, respectively.

14

---

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The Company uses the Monte-Carlo simulation model to determine the fair value and the derived service period of performance-based option awards, with market conditions, on the date of the grant.

**ESPP**

The weighted-average estimated per share fair value of shares purchased under the Company's ESPP was \$0.59 and \$1.62 during the three months ended March 31, 2015 and 2014, respectively.

The weighted-average estimated per share fair value of shares purchased under the Company's ESPP was \$1.02 and \$1.44 during the nine months ended March 31, 2015 and 2014, respectively.

Excluding the options assumed as part of the Enterasys acquisition, the fair value of each option award and share purchase option under the Company's ESPP is estimated on the date of grant using the Black-Scholes-Merton option valuation model with the weighted average assumptions noted in the following table.

	Stock Option Plan		Employee Stock Purchase Plan		Stock Option Plan		Employee Stock Purchase Plan		
	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014	Nine Months Ended March 31, 2015	Nine Months Ended March 31, 2014	Nine Months Ended March 31, 2015	Nine Months Ended March 31, 2014	
Expected life	4.6 years	5.0 years	0.50 years	0.25 years	4.7 years	4.0 years	0.33 years	0.25 years	
Risk-free interest rate	1.49 %	1.41 %	0.07 %	0.09 %	1.60 %	1.23 %	0.04 %	0.10 %	%
Volatility	54 %	57 %	58 %	57 %	54 %	56 %	58 %	51 %	%
Dividend yield	— %	— %	— %	— %	— %	— %	— %	— %	%

**8. Commitments and Contingencies****Purchase Commitments**

The Company currently has arrangements with contract manufacturers and suppliers for the manufacture of its products. The arrangements allow them to procure long lead-time component inventory based upon a rolling production forecast provided by the Company. The Company is obligated to the purchase of long lead-time component inventory that its contract manufacturer procures in accordance with the forecast, unless the Company gives notice of order cancellation outside of applicable component lead-times. The Company had non-cancelable commitments to purchase \$100.7 million of such inventory as of March 31, 2015.

**Legal Proceedings**

The Company may from time to time be party to litigation arising in the course of its business, including, without limitation, allegations relating to commercial transactions, business relationships or intellectual property rights. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources. Litigation in general and intellectual property and securities litigation in particular, can be expensive and disruptive to normal business operations. Moreover, the results of legal proceedings are difficult to predict.

In accordance with applicable accounting guidance, the Company records accruals for certain of its outstanding legal proceedings, investigations or claims when it is probable that a liability will be incurred and the amount of loss can be reasonably estimated. The Company evaluates, at least on a quarterly basis, developments in legal proceedings, investigations or claims that could affect the amount of any accrual, as well as any developments that would result in a loss contingency to become both probable

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

and reasonably estimable. When a loss contingency is not both probable and reasonably estimable, the Company does not record a loss accrual. However, if the loss (or an additional loss in excess of any prior accrual) is at least a reasonable possibility and material, then the Company would disclose an estimate of the possible loss or range of loss, if such estimate can be made, or disclose that an estimate cannot be made. The assessment whether a loss is probable or a reasonable possibility, and whether the loss or a range of loss is estimable, involves a series of complex judgments about future events. Even if a loss is reasonably possible, the Company may not be able to estimate a range of possible loss, particularly where (i) the damages sought are substantial or indeterminate, (ii) the proceedings are in the early stages, or (iii) the matters involve novel or unsettled legal theories or a large number of parties. In such cases, there is considerable uncertainty regarding the ultimate resolution of such matters, including the amount of any possible loss, fine or penalty. Accordingly, for current proceedings, except as noted below, the Company is currently unable to estimate any reasonably possible loss or range of possible loss. However, an adverse resolution of one or more of such matters could have a material adverse effect on the Company's results of operations in a particular quarter or fiscal year.

## Litigation

## Commonwealth of Kentucky

On or about February 3, 2014, a class action lawsuit was filed in the Commonwealth of Kentucky against Enterasys Networks, Inc. and two other defendants. The complaint alleges that Enterasys and its subcontractor, TJI Information Technologies, Inc., d.b.a. Unbridled Information Technologies (“Subcontractor”), violated Kentucky’s wage and hour laws and failed to pay the prevailing wage in violation of the Kentucky State Prevailing Wage Act (the “Act”) on various public works projects for a number of Kentucky government agencies since January 2010. Plaintiffs also allege common law actions for quantum merit and unjust enrichment and they seek monetary damages, costs, expenses and attorney fees, although there was no quantified amount identified. One of the defendants, Integrated Facility Systems, LLC (“IFS”), has also filed a cross-claim against Enterasys. The Company denies the claims and filed answers to both the complaint and cross-claim on April 16, 2014. In addition, the Company filed a cross-claim for indemnity against IFS.

Plaintiffs filed a first amended complaint on September 26, 2014, in which they named Commonwealth of Kentucky’s Office of Technology under the State’s Finance and Administration Cabinet (“COT”) as a defendant. The Company filed an answer to the Plaintiffs’ first amended complaint on October 10, 2014. COT then filed a motion to dismiss COT as a defendant in this lawsuit and the court granted COT’s motion. Plaintiffs filed a motion for Summary Judgment/Adjudication on the issue of whether the work performed by the defendants constitutes “construction” under the Act, which was denied on February 26, 2015. Given the preliminary nature of the lawsuit, it is premature to assess the likelihood of a particular outcome.

## ICMS Tax Assessment Matters

The State of Sao Paulo (Brazil) denied Enterasys Networks do Brazil Ltda. the use of certain credits derived from the State of Espirito Santo under the terms of the FUNDAP scheme for the tax years of 2002 through 2009. Enterasys’ application to resolve the ICMS Tax Assessments at the administrative level of the Sao Paulo Tax Department under the amnesty relief program (Reference No 3.056.963-1) was denied in March, 2014, by the Sao Paulo Tax Administration. The value of the ICMS tax credits that were disallowed by the Sao Paulo Tax Administration is approximately BR 3,443,914 (or approximately US \$1.5 million), plus interest and penalties (that are currently estimated to be approximately US \$9.0 million). On January 10, 2014, Enterasys filed a lawsuit to overturn or reduce the assessment, which lawsuit remains on-going. As part of this lawsuit, Enterasys made a request for a stay of execution, so that no tax foreclosure can be filed until a final ruling is made and no guarantee needs to be presented. On or about October 6, 2014, the preliminary injunction was granted with regard to the stay of execution, and in

response to an appeal on the guarantee requirement, the appellant court further ruled on or about January 28, 2015 that no cash deposit (or guarantee) need be made by Enterasys.

Given the preliminary nature of the lawsuit, it is premature to assess the likelihood of a particular final outcome.

Based on the currently available information, the Company believes the ultimate outcome of this audit will not have material adverse effect on the Company's financial position or overall trends in results of operations. The range of the potential total tax liability related to these matters is estimated to be from US \$0 million to US \$9.0 million, of which the Company believes US \$4.3 million is the best estimate within the range and has recorded an accrual as of the acquisition date of Enterasys as such matter relates to the period before the acquisition.

Unify U.S. Holdings, Inc. (formerly known as Enterprise Networks Holdings, Inc.).

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

On or about April 8, 2015, Company filed a lawsuit against Unify U.S. Holdings, Inc. (formerly known as Enterprise Networks Holdings, Inc.) (“Seller”) for breach of, and indemnification by Seller under, the purchase agreement, between Seller and Company, for Company’s purchase of Enterasys Networks, Inc. and its subsidiaries (the “Purchase Agreement”). The complaint alleges numerous claims for indemnification resulting from Seller’s violations of certain clauses in the Purchase Agreement and Seller’s failure to make accurate and proper disclosures as required by the Purchase Agreement. The Company was compelled to file this action to perfect and preserve the Company’s right to indemnification by Seller under the Purchase Agreement. Although the Company’s complaint has not quantified the amount being sought, the complaint seeks, among other things, monetary damages, costs, expenses and attorney fees in connection with each of the claims. Given the preliminary nature of the lawsuit, it is premature to assess the likelihood of a particular or final outcome.

Wetro LAN LLC

On Mar 23, 2015, Wetro LAN LLC (Wetro), a non-practicing entity, filed a complaint against Extreme in the Eastern District of Texas asserting infringement of United States Patent No. 6,795,918 (the “ ‘918 Patent”). Wetro alleges that Extreme “makes, uses, provides, offers for sale, and sells their product entitled Extreme Networks- Altitude 4700 Series Access Points and similarly situated wireless routers” and thereby has infringed the 918 Patent. Wetro sued a number of other technology companies in January and February 2015 for the same patent. Indications at the USPTO are that the 918 Patent has expired, limiting potential damages including all future damages in the case. Wetro seeks monetary damages, although the complaint seeks no quantified amount. Given the preliminary nature of the lawsuit, it is premature to assess the likelihood of a particular or final outcome.

## 9. Income Taxes

The Company recorded an income tax provision of \$1.1 million and \$3.5 million, for the three and nine months ended March 31, 2015, respectively. The Company recorded an income tax provision of \$0.9 million and \$2.3 million for the three and nine months ended March 31, 2014, respectively.

The income tax provisions for the three and nine months ended March 31, 2015 and 2014, consisted primarily of taxes on the income of our foreign subsidiaries as well as tax expense associated with the establishment of a U.S. deferred tax liability for amortizable goodwill resulting from the acquisition of Enterasys Networks, Inc. The income tax provisions for both fiscal years were calculated based on the actual results of operations for the three and nine months ended March 31, 2015 and 2014, and therefore may not reflect the annual effective tax rate.

The Company has provided a full valuation allowance against all of its U.S. federal and state deferred tax assets as well as substantially all of the acquired Enterasys foreign entities’ deferred tax assets. No valuation allowance has been established against the non-U.S. deferred tax assets of the legacy Extreme Networks, Inc. foreign subsidiaries. A valuation allowance is determined by assessing both negative and positive evidence to determine whether it is “more likely than not” that the deferred tax assets are recoverable; such assessment is required on a jurisdiction by jurisdiction basis. The Company's inconsistent earnings in recent periods, coupled with the Company's inability to forecast greater than one quarter in advance and the cyclical nature of its business represent sufficient negative evidence to require a full valuation allowance against its U.S. federal and state net deferred tax assets as well as the above mentioned foreign jurisdictions. This valuation allowance will be evaluated periodically and can be reversed partially or in whole if business results and the economic environment have sufficiently improved to support realization of some or all of the Company's deferred tax assets.

The acquisition of Enterasys included a U.S. parent company as well as its wholly-owned domestic and foreign subsidiaries. The Company has elected to treat this stock acquisition as an asset purchase by filing the required election forms under IRC Sec 338(h)(10). The Company has estimated the value of the intangible assets from this transaction and is amortizing the amount over 15 years for tax purposes. The Company deducted \$1.1 million and \$3.4

million, during the three and nine months ended March 31, 2015, respectively of tax amortization expense related to capitalized goodwill. The Company recorded a deferred tax liability of \$2.4 million related to this amortization which is not considered a future source of taxable income in evaluating the need for a valuation allowance against our deferred tax assets as of March 31, 2015.

The Company had \$11.3 million of unrecognized tax benefits as of March 31, 2015. The future impact of the unrecognized tax benefit of \$11.3 million, if recognized, would result in adjustments to deferred tax assets and corresponding adjustments to the valuation allowance. The Company does not anticipate any events to occur during the next twelve months that would reduce the unrealized tax benefit as currently stated in the Company's balance sheet. Estimated interest and penalties related to the underpayment of income taxes are classified as a component of tax expense in the Condensed Consolidated Statements of Operations and were immaterial for the three and nine months ended March 31, 2015 and 2014. Accrued interest and penalties were \$42,000 as of March 31, 2014, and have been fully reversed as of March 31, 2015.

Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

In general, the Company's U.S. federal income tax returns are subject to examination by tax authorities for fiscal years 2001 forward due to net operating losses and the Company's state income tax returns are subject to examination for fiscal years 2003 forward due to net operating losses.

## 10. Net Loss Per Share

Basic earnings per share is calculated by dividing net earnings by the weighted average number of common shares outstanding during the period. Dilutive earnings per share is calculated by dividing net earnings by the weighted average number of common shares used in the basic earnings per share calculation plus the dilutive effect of shares subject to repurchase, options, warrants and unvested restricted stock.

The following table presents the calculation of basic and diluted net loss per share (in thousands, except per share data):

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Net loss	\$(23,548 )	\$(25,058 )	\$(55,983 )	\$(41,079 )
Weighted-average shares used in per share calculation – basic and diluted	99,783	96,069	98,591	95,116
Net loss per share – basic and diluted	\$(0.24 )	\$(0.26 )	\$(0.57 )	\$(0.43 )

The following securities were excluded from the computation of diluted net loss per share of common stock for the periods presented as their effect would have been anti-dilutive (in thousands):

	March 31, 2015	March 31, 2014
Options to purchase common stock	9,839	7,171
Restricted stock units	1,694	1,038

## 11. Foreign Exchange Forward Contracts

The Company uses derivative financial instruments to manage exposures to foreign currency. The Company's objective for holding derivatives is to use the most effective methods to minimize the impact of these exposures. The Company does not enter into derivatives for speculative or trading purposes. The Company records all derivatives on the balance sheet as "Other assets" at fair value. Changes in the fair value of derivatives are recognized in earnings as Other Income (Expense). The Company from time to time enters into foreign exchange forward contracts to mitigate the effect of gains and losses generated by the foreign currency forecast transactions related to certain operating expenses and re-measurement of certain assets and liabilities denominated in foreign currencies. These derivatives do not qualify as hedges. As of March 31, 2015, the Company did not have any foreign currency contracts.

Foreign currency transaction gains and losses from operations was a loss of \$0.5 million and \$0.1 million for the three months ended March 31, 2015 and 2014, respectively. Foreign currency transaction gains and losses from operations were a loss of \$0.9 million and \$1.2 million for the nine months ended March 31, 2015 and 2014, respectively.

## 12. Disclosure about Segments of an Enterprise and Geographic Areas

The Company operates in one segment, the development and marketing of network infrastructure equipment. The Company conducts business globally and is managed geographically. Revenue is attributed to a geographical area based on the location of





Table of Contents

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

its customers. The Company operates in three geographical areas: Americas; which includes the United States, Canada, Mexico, Central America and South America; Europe, the Middle East and Africa ("EMEA"); which includes Europe, Russia, the Middle East and Africa; and APAC; which includes Asia Pacific, South Asia, India, Australia and Japan.

The Company attributes revenues to geographic regions primarily based on the customer's ship-to location.

Information regarding geographic areas is as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	March 31, 2015	March 31, 2014	March 31, 2015	March 31, 2014
Net Revenues:				
Americas:				
United States	\$49,353	\$59,896	\$166,001	\$141,576
Other	7,073	12,082	26,990	37,816
Total Americas	56,426	71,978	192,991	179,392
EMEA	50,006	54,113	166,515	146,175
APAC	13,158	15,671	43,566	38,694
Total net revenues	\$119,590	\$141,762	\$403,072	\$364,261
Long Lived Assets:			March 31, 2015	June 30, 2014
Americas			\$93,185	\$104,387
EMEA			32,773	45,191
APAC			3,312	3,121
Total long lived assets			\$129,270	\$152,699

Table of Contents

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This quarterly report on Form 10-Q, including the following sections, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including in particular, our expectations regarding market demands, customer requirements and the general economic environment, future results of operations, and other statements that include words such as "may" "expect" or "believe" . These forward-looking statements involve risks and uncertainties. We caution investors that actual results may differ materially from those projected in the forward-looking statements as a result of certain risk factors identified in the section entitled "Risk Factors" in this Report, our Quarterly Report on Form 10-Q for the third quarter of fiscal 2015, our Annual Report on Form 10-K for the fiscal year ended June 30, 2014, and other filings we have made with the Securities and Exchange Commission. These risk factors, include, but are not limited to: fluctuations in demand for our products and services; a highly competitive business environment for network switching equipment; our effectiveness in controlling expenses; the possibility that we might experience delays in the development or introduction of new technology and products; customer response to our new technology and products; the timing of any recovery in the global economy; risks related to pending or future litigation; a dependency on third parties for certain components and for the manufacturing of our products; and our ability to receive the anticipated benefits of the acquisition of Enterasys.

Business Overview

We are a leading provider of network infrastructure equipment and services for enterprises, data centers, and service providers. We were incorporated in California in May 1996, and reincorporated in Delaware in March 1999. The shares of Extreme Networks, Inc. ("EXTR") began trading on NASDAQ in April 1999. Our corporate headquarters are located in San Jose, California. We develop and sell network infrastructure equipment to our enterprise, data center and telecommunications service provider customers.

On October 31, 2013 (the "Acquisition Date"), we completed the acquisition of Enterasys Networks, Inc. ("Enterasys"), a privately held provider of wired and wireless network infrastructure and security solutions, for \$180.0 million, net of cash acquired, whereby Enterasys became our wholly-owned subsidiary. The combined entity immediately became a networking industry leader with more than 14,000 customers. As a combined Company, we believe we will set the standard for the networking industry with a strategic focus on three principles:

**Highly scaled and differentiated products and solutions:** Our combined product portfolio spans data center networking, switching and routing, Software-Defined Networking ("SDN"), wired and wireless LAN access, network management with analytics and integrated security features. This broader solutions portfolio can be leveraged to better serve existing and new customers. We will continue to enhance and support the product roadmaps of both companies going forward to protect the investments of customers and avoid any disruption to their businesses. We intend to increase research and development to accelerate our vision for high-performance, modular, open networking.

**Leading customer service and support:** We are working to augment our current outsourced support model by integrating Enterasys' in-sourced expertise, building on Enterasys' award-winning heritage and strong commitment to exceptional customer experience. The Company's expanded global network of channel partners and distributors will benefit from expanded services and support capabilities.

**Strong Channels and Strategic Partners:** Our focus is to leverage the capabilities of the combined Company and expand existing partnerships with Ericsson and the developing partnership with Lenovo as well as continue to add new strategic partnerships in the future. Additionally, we will increase our focus on partnering with distributors and channel partners globally. The goal is to develop and enhance relationships that grow revenue and profits for the Company and our alliance and channel partners. At the same time, we are investing in infrastructure to make doing business with the Company easier and more efficient.

We conduct our sales and marketing activities on a worldwide basis through a distribution channel utilizing distributors, resellers and our field sales organization. We primarily sell our products through an ecosystem of channel

partners who combine our Ethernet, wireless and software analytics products with their offerings to create compelling information technology solutions for end-user customers. We utilize our field sales organization to support our channel partners and to sell direct to end-user customers, including some large global accounts. Our customers include businesses, hospitals, hotels, universities, sports venues, telecommunications companies and government agencies around the world.

20

---

## Table of Contents

We outsource the majority of our manufacturing and supply chain management operations as part of our strategy to maintain global manufacturing capabilities and to reduce our costs. We conduct quality assurance, manufacturing engineering, document control and test development at engineering facilities in San Jose, California; Research Triangle Park, North Carolina; Salem, New Hampshire; Toronto, Canada and Chennai, India. This approach enables us to reduce fixed costs and to flexibly respond to changes in market demand.

The market for network infrastructure equipment is highly competitive and dominated by a few large companies. The current economic climate has further driven consolidation of vendors within the Ethernet networking market and with vendors from adjacent markets, including storage, security, wireless and voice applications. We believe that the underpinning technology for all of these adjacent markets is Ethernet. As a result, we believe that, as an independent Ethernet switch vendor, we must provide products that, when combined with the products of our large strategic partners, create compelling solutions for end user customers. Our approach is to focus on the intelligence and automation layer that spans our hardware and software products that facilitates end-to-end solutions, as opposed to positioning Extreme Networks as a low-cost-vendor with point products.

We believe that continued success in our marketplace is dependent upon a variety of factors that includes, but is not limited to, our ability to design, develop and distribute new and enhanced products employing leading-edge technology.

### Critical Accounting Policies and Estimates

Our unaudited condensed consolidated financial statements and the related notes included elsewhere in this report are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these unaudited condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. In many instances, we could have reasonably used different accounting estimates, and in other instances changes in the accounting estimates are reasonably likely to occur from period to period. Accordingly, actual results could differ significantly from the estimates made by our management. On an ongoing basis, we evaluate our estimates and assumptions. To the extent that there are material differences between these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected.

As discussed in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of our Annual Report on Form 10-K for the year ended June 30, 2014, we consider the following accounting policies to be the most critical in understanding the judgments that are involved in preparing our consolidated financial statements:

- Revenue Recognition
- Business Combinations
- Goodwill
- Share-based Payments
- Deferred Tax Valuation Allowance
- Accounting for Uncertainty in Income Taxes

There have been no changes to our critical accounting policies since the filing of our last Annual Report on Form 10-K.

### New Accounting Pronouncements

See Note 3 of the accompanying condensed consolidated financial statements for a full description of new accounting pronouncements, including the respective expected dates of adoption and effects on results of operations and financial condition.

### Liquidity and Capital Resources

The following summarizes information regarding our cash, investments, and working capital (in thousands):



Table of Contents

	March 31, 2015	June 30, 2014
Cash and cash equivalent	\$74,067	\$73,190
Investments	1,506	32,692
Total cash and investments	\$75,573	\$105,882
Working capital	\$8,755	\$56,548

As of March 31, 2015, our principal sources of liquidity consisted of cash, cash equivalents and investments of \$75.6 million, net accounts receivable of \$78.7 million and \$1.0 million of letters of credit and borrowings from the Revolving Facility under which we had \$8.6 million of additional availability as of March 31, 2015. Our principal uses of cash will include purchase of finished goods inventory from our contract manufacturers, payroll and other operating expenses related to the development and marketing of our products, purchases of property and equipment, repayments of debt and related interest. We believe that our \$75.6 million of cash and cash equivalents and investments as of March 31, 2015, along with the availability of borrowings from the Revolving Facility will be sufficient to fund our principal uses of cash for at least the next 12 months.

Our Credit Agreement contains financial covenants that require us to maintain a minimum Consolidated Fixed Charge Coverage Ratio, a Consolidated Quick Ratio and a maximum Consolidated Leverage Ratio and several other covenants and restrictions that limit our ability to incur additional indebtedness, create liens upon any of our property, merge, consolidate or sell all or substantially all of our assets, etc. During the three months ended December 31, 2014, we amended the Credit Agreement and among other things modified certain financial covenants governing the Quick and Leverage ratios.

The Credit Agreement also includes customary events of default, including failure to pay principal, interest or fees when due, failure to comply with covenants, if any representation or warranty made by us is false or misleading in any material respect, certain insolvency or receivership events affecting Extreme and its subsidiaries, the occurrence of certain material judgments, the occurrence of certain ERISA events, the invalidity of the loan documents or a change in control of our Company. The amounts outstanding under the Credit Agreement may be accelerated upon certain events of default. We believe we are in compliance and expect to remain in compliance with our Credit Agreement covenants and they are not expected to impact our liquidity or capital resources.

**Key Components of Cash Flows and Liquidity**

A summary of the sources and uses of cash and cash equivalents is as follows (in thousands):

	Nine Months Ended	
	March 31, 2015	March 31, 2014
Net cash provided by (used in) operating activities	\$33,564	\$(30,617 )
Net cash provided by (used in) investing activities	21,687	(123,113 )
Net cash (used in) provided by financing activities	(50,607 )	128,671
Foreign currency effect on cash	(3,767 )	611
Net increase (decrease) in cash and cash equivalents	\$877	\$(24,448 )
Net Cash Provided by (Used In) Operating Activities		

Cash flows provided by operations was \$33.6 million in the nine months ending March 31, 2015. Current period's net loss was primarily offset by non-cash expenses such as amortization of intangibles, stock-based compensation expense and depreciation. Accounts receivables decreased primarily due to lower sales during the current quarter and to our higher collections efforts. Inventories increased primarily due to the reduced sales during the third quarter. Accounts payable increased due to timing of payments. The increases in cash inflows were offset by decreases in accrued compensation due to lower commissions and bonus accruals.

Cash flows used in operations was \$30.6 million in the nine months ending March 31, 2014. The net loss for the period was primarily offset by non-cash expenses such as amortization of intangibles, stock-based compensation

expense and depreciation. Accounts receivables, inventory and accounts payables primarily increased due to increased activity post acquisition.



Table of Contents

## Net Cash Provided by (Used In) Investing Activities

Cash flow provided by investing activities was \$21.7 million, in the nine months ending March 31, 2015, primarily comprised of proceeds from the sale and maturities of investments of \$9.1 million and \$21.8 million of investments, respectively, offset by \$5.6 million used to purchase property and equipment and \$3.0 million used to acquire a non-marketable equity interest.

Cash flow used in investing activities was \$127.0 million in the nine months ending March 31, 2014, comprised of \$180.0 million net cash used in the acquisition of Enterasys, purchases of investments of \$9.0 million, \$12.6 million used to purchase property and equipment offset by proceeds of \$20.1 million from the maturities of investments and proceeds of \$54.6 million from the sale of investments.

## Net Cash (Used In) Provided by Financing Activities

Cash flow used in financing activities was \$50.6 million in the nine months ending March 31, 2015, comprised of \$77.1 million of cash used for repayment of debt offset by a draw on the Revolving Facility of \$24 million during the nine months ended March 31, 2015, for working capital requirements, \$2.5 million proceeds from the exercise of stock options and issuance of shares of our common stock under the ESPP, net of taxes paid on vested and released stock awards.

Cash flow provided by financing activities was \$104.0 million in the nine months ending March 31, 2014, comprised of the issuance of a Term Loan of \$65.0 million and a draw on the Revolving Facility of \$35 million used for the acquisition of Enterasys, \$4.8 million proceeds from the exercise of stock options and issuance of shares of our common stock under the ESPP, net of taxes paid on vested and released stock awards offset by \$0.8 million of cash used for repayment of debt.

## Foreign currency effect on cash

Foreign currency effect on cash increased in the nine months ending March 31, 2015, primarily due to the strengthening US Dollar and the resulting changes in foreign currency exchange rates between the US Dollar and particularly the Euro, Great Britain Pound, Brazilian Real, Swedish Krona, Indian Rupee and Australian Dollar.

## Contractual Obligations

The following summarizes our contractual obligations as of March 31, 2015, and the effect such obligations are expected to have on our liquidity and cash flow in future periods (in thousands):

	Total	Less than 1 Year	1-3 years	3-5 years	More than 5 years
Contractual Obligations:					
Debt obligations	\$68,500	\$9,750	\$37,375	\$21,375	\$—
Interest on debt obligations	4,628	1,834	2,488	306	—
Non-cancellable inventory purchase commitments	100,693	100,693	—	—	—
Non-cancellable operating lease obligations	66,040	10,681	18,630	16,934	19,795
Other liabilities	8,703	5,859	2,701	143	—
Total contractual cash obligations	\$248,564	\$128,817	\$61,194	\$38,758	\$19,795

Non-cancellable inventory purchase commitments represent the purchase of long lead-time component inventory that our contract manufacturers procure in accordance with our forecast. Inventory purchase commitments were \$100.7 million as of March 31, 2015. We expect to honor the inventory purchase commitments within the next 12 months. Non-cancellable operating lease obligations represent base rents and operating expense obligations to landlords for facilities we occupy at various locations.

Other liabilities include our commitments towards debt related fees and specific arrangements other than inventory. The amounts in the table above exclude immaterial income tax liabilities related to uncertain tax positions as we are unable to reasonably estimate the timing of settlement.

We did not have any material commitments for capital expenditures as of March 31, 2015.

## Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of March 31, 2015.



Table of Contents

## Results of Operations

During the third quarter of fiscal 2015, we experienced the following results:

Net revenues of \$119.6 million compared to net revenues of \$141.8 million in the third quarter of fiscal 2014.

Product revenues of \$86.5 million compared to product revenues of \$109.9 million in the third quarter of fiscal 2014.

Service revenues of \$33.1 million compared to service revenues of \$31.9 million in the third quarter of fiscal 2014.

Total gross margin of 48.3% of net revenues compared to total gross margin of 50.0% of net revenues in the third quarter of fiscal 2014.

Operating loss of \$21.3 million compared to operating loss of \$23.4 million in the third quarter of fiscal 2014.

Net loss of \$23.5 million compared to net loss of \$25.1 million in the third quarter of fiscal 2014.

Cash flow provided by operating activities of \$33.6 million in the nine months ended March 31, 2015 compared to cash flow used in operating activities of \$30.6 million in the nine months ended March 31, 2014.

Cash and cash equivalents, short-term investments and marketable securities decreased by \$30.3 million to \$75.6 million as of March 31, 2015 from \$105.9 million as of June 30, 2014, primarily due to repayment of debt offset by cash provided by operations and investing activities.

We operate in three regions: Americas; which includes the United States, Canada, Mexico, Central America and South America; EMEA; which includes Europe, Russia, Middle East, and Africa; and APAC; which includes Asia Pacific, South Asia, India, and Australia.

The following table presents the total net revenue geographically for the three and nine months ended March 31, 2015 and March 31, 2014 (dollars in thousands):

Net Revenues	Three Months Ended				Nine Months Ended				
	March 31, 2015	March 31, 2014	\$ Change	% Change	March 31, 2015	March 31, 2014	\$ Change	% Change	
Americas:									
United States	\$49,353	\$59,896	\$(10,543)	(17.6)%	\$166,001	\$141,576	\$24,425	17.3%	
Other	7,073	12,082	(5,009)	(41.5)%	26,990	37,816	(10,826)	(28.6)%	
Total Americas	56,426	71,978	(15,552)	(21.6)%	192,991	179,392	13,599	7.6%	
Percentage of net revenue	47.0%	50.8%			47.9%	49.2%			
EMEA	50,006	54,113	(4,107)	(7.6)%	166,515	146,175	20,340	13.9%	
Percentage of net revenue	41.8%	38.2%			41.3%	40.1%			
APAC	13,158	15,671	(2,513)	(16.0)%	43,566	38,694	4,872	12.6%	
Percentage of net revenue	11.0%	11.1%			10.8%	10.6%			
Total net revenues	\$119,590	\$141,762	\$(22,172)	(15.6)%	\$403,072	\$364,261	\$38,811	10.7%	

## Net Revenues

The following table presents net product and service revenue for the three and nine months ended March 31, 2015 and March 31, 2014 (dollars in thousands):

Table of Contents

	Three Months Ended				Nine Months Ended				
	March 31, 2015	March 31, 2014	\$ Change	% Change	March 31, 2015	March 31, 2014	\$ Change	% Change	
Net Revenues:									
Product	\$86,527	\$109,891	\$(23,364)	(21.3)%	\$301,700	\$290,001	\$11,699	4.0%	
Percentage of net revenue	72.4	% 77.5	%		74.9	% 79.6	%		
Service	33,063	31,871	1,192	3.7%	101,372	74,260	27,112	36.5%	
Percentage of net revenue	27.7	% 22.5	%		25.1	% 20.4	%		
Total net revenues	\$119,590	\$141,762	\$(22,172)	(15.6)%	\$403,072	\$364,261	\$38,811	10.7%	

Product revenue decreased \$23.4 million or 21.3% in the three months ended March 31, 2015, compared to the corresponding period of fiscal 2014. In the Americas, we experienced deferred spending in our overall customer base as well as our overall deal sizes were smaller during the 2015 period compared to corresponding period of fiscal 2014. The strengthening United States Dollar, especially against currencies in Europe and South America, resulted in customers delaying purchases or customers executing transactions at lower than expected spending levels.

Product revenue increased \$11.7 million or 4.0% in the nine months ended March 31, 2015, compared to the corresponding period of fiscal 2014. The fiscal 2015 period reflects increased product shipments and customers as a result of our acquisition of Enterasys for the full nine months. Whereas the fiscal 2014 period only reflects five months of sales subsequent to the October 31, 2013 acquisition date. However, the increase in sales was partially offset by declines of customer spending across each geographical region and an increase in customer discounts. The decline in customer spending was partially due to the significant strengthening of the United States Dollar in all geographical areas and the entrance of competitors in regions where we have a strong presence, specifically in Asia Pacific and EMEA regions.

Service revenue increased \$1.2 million or 3.7% for the three months ended March 31, 2015 compared to the corresponding period of fiscal 2014 due to an increase in service maintenance contracts and professional service and training revenues due to our acquisition of Enterasys. Additionally, purchase accounting charges related to deferred service revenues decreased \$1.1 million for the three months ended March 31, 2015, as compared to the corresponding period of fiscal 2014.

Service revenue increased \$27.1 million or 36.5% for the nine months ended March 31, 2015 compared to the corresponding period of fiscal 2014 due to an increase in service maintenance contracts and professional service and training revenues due to our acquisition of Enterasys. Purchase accounting charges related to deferred service revenues decreased \$1.4 million for the nine months ended March 31, 2015 as compared to the corresponding period of fiscal 2014.

**Gross Profit**

The following table presents our product and service revenue gross profit and the respective gross profit percentages for the three and nine months ended March 31, 2015 and 2014 (dollars in thousands):

	Three Months Ended				Nine Months Ended				
	March 31, 2015	March 31, 2014	\$ Change	% Change	March 31, 2015	March 31, 2014	\$ Change	% Change	
Gross profit:									
Product	\$36,766	\$51,188	\$(14,422)	(28.2)%	\$137,418	\$136,889	\$529	0.4%	
Percentage of product revenue	42.5	% 46.6	%		45.5	% 47.2	%		
Service	20,958	19,667	1,291	6.6%	65,995	47,518	18,477	38.9%	

Edgar Filing: EXTREME NETWORKS INC - Form 10-Q

Percentage of service revenue	63.4	%	61.7	%		65.1	%	64.0	%
Total gross profit	\$57,724		\$70,855		\$(13,131 ) (18.5 )%	\$203,413		\$184,407	\$19,006 10.3 %
Percentage of net revenue	48.3	%	50.0	%		50.5	%	50.6	%

Cost of product revenue includes costs of materials, amounts paid to third-party contract manufacturers, costs related to warranty obligations, charges for excess and obsolete inventory, amortization expense for developed technology, royalties under technology license agreements, and internal costs associated with manufacturing overhead, including management, manufacturing engineering, quality assurance, development of test plans, and document control. We outsource substantially all of our

Table of Contents

manufacturing and supply chain management operations, and we conduct quality assurance, manufacturing engineering, document control and distribution in San Jose, California; Salem, New Hampshire; China, and Taiwan. Product gross profit decreased \$14.4 million in the three months ended March 31, 2015, as compared to the corresponding period of fiscal 2014. Gross profit was impacted during the third quarter of fiscal 2015 by a decrease of \$23.4 million in product revenue and higher material costs, an increase of \$3.2 million in excess and obsolete inventory charges and \$0.7 million in distribution expenses due to higher utilization of air freight charges as compared to the corresponding period of fiscal 2014.

Product gross profit increased to \$137.4 million in the nine months ended March 31, 2015, from \$136.9 million in the corresponding period of fiscal 2014. Product gross profit for the nine months ended March 31, 2014, was favorably impacted by an increase in product revenue of \$35.2 million, offset by higher material costs, an increase of \$5.8 million in excess and obsolete inventory charges, \$5.6 million for amortization of the developed technology intangibles from the acquisition of Enterasys, \$2.3 million for distribution costs, due to higher utilization of air freight charges and \$1.2 million of warranty reserves. Gross profit for the first nine months of fiscal 2014, was negatively impacted by \$11.1 million related to the sale of inventory which had been adjusted to fair value upon the Enterasys acquisition due to purchase accounting.

Our cost of service revenue consists primarily of personnel, overhead, repair and freight costs and the cost of spares used in providing support under customer service contracts.

Service gross profit increased to \$21.0 million in the three months ended March 31, 2015, from \$19.7 million in the corresponding of fiscal 2014. The increase in service gross profit was primarily due to lower purchase accounting charges related to deferred service revenues of \$1.1 million for the three months ended March 31, 2015, as compared to the three months ended March 31, 2014.

Service gross profit increased to \$66.0 million for the nine months ended March 31, 2015, from \$47.5 million in the corresponding period of fiscal 2014, primarily due to increase in service revenue of \$27.1 million partially offset by increased personnel, overhead and travel costs as a result of the acquisition of Enterasys. Additionally, purchase accounting charges related to deferred service revenues decreased \$1.4 million in fiscal 2015 as compared to fiscal 2014.

Operating Expenses

The following table presents operating expenses and operating income (dollars in thousands):

	Three Months Ended				Nine Months Ended				
	March 31, 2015	March 31, 2014	\$ Change	% Change	March 31, 2015	March 31, 2014	\$ Change	% Change	
Research and development	\$23,858	\$24,265	\$(407)	(1.7)%	\$71,205	\$53,098	\$18,107	34.1%	
Sales and marketing	39,226	44,703	(5,477)	(12.3)%	127,976	108,033	19,943	18.5%	
General and administrative	9,711	11,178	(1,467)	(13.1)%	31,091	29,301	1,790	6.1%	
Acquisition and integration costs	1,725	6,443	(4,718)	(73.2)%	9,283	18,826	(9,543)	(50.7)%	
Restructuring charge, net of reversals	—	(6)	6	(100.0)%	—	499	(499)	(100.0)%	
Amortization of intangibles	4,467	7,666	(3,199)	(41.7)%	13,402	11,444	1,958	17.1%	
Total operating expenses	\$78,987	\$94,249	\$(15,262)	(16.2)%	\$252,957	\$221,201	\$31,756	14.4%	
Operating loss	\$(21,263)	\$(23,394)	\$2,131	9.1%	\$(49,544)	\$(36,794)	\$(12,750)	(34.7)%	

Research and Development Expenses

Research and development expenses consist primarily of salaries and related personnel expenses, consultant fees and prototype expenses related to the design, development, and testing of our products.

Research and development expenses decreased by \$0.4 million for the three months ended March 31, 2015 as compared to the corresponding period of fiscal 2014. The comparison for the three month period were relatively flat due to the completion

## Table of Contents

of the integration of Enterasys. An increase of \$0.9 million in personnel costs, \$0.2 million in facilities costs and \$0.2 million in depreciation, were offset by \$1.4 million in reductions of engineering and software expenses.

Research and development increased by \$18.1 million or 34.1% for the nine months ended March 31, 2015. The increase in research and development expense for the nine month period were primarily due to increased spending as a result of our acquisition of Enterasys. The increase in spending were \$17.4 million of personnel costs, which includes compensation, benefits and non-cash stock based compensation, \$1.0 million in depreciation and \$0.8 million for supplies and equipment.

### Sales and Marketing Expenses

Sales and marketing expenses consist of salaries, commissions and related expenses for personnel engaged in marketing and sales functions, as well as trade shows and promotional expenses.

Sales and marketing expenses decreased by \$5.5 million, or 12.3% for the three months ended March 31, 2015, as compared to the corresponding period of fiscal 2014. The decrease in sales and marketing expense for the three month period of fiscal 2015 were primarily due to lower compensation and benefits of \$3.8 million due to reduced headcount, \$0.4 million in professional fees and \$0.3 million in facilities expense. The decrease in sales and marketing expenses was also partially due to the strengthening United States Dollar.

Sales and marketing increased by \$19.9 million or 18.5% for the nine months ended March 31, 2015, as compared to the corresponding period of fiscal 2014. The increase in sales and marketing expenses during the nine month period of fiscal 2015 was primarily due to \$11.4 million of higher compensation and benefits, including non-cash stock compensation, \$1.7 million in facilities. \$1.4 million in travel. This was partially offset with a reduction of \$1.7 million in marketing expense. All of these factors were driven by the acquisition of Enterasys.

### General and Administrative Expenses

General and administrative expense consists primarily of personnel costs, legal and professional service costs, share-based compensation, travel and facilities and information technology costs.

General and administrative expenses decreased by \$1.5 million, or 13.1% for the three months ended March 31, 2015, as compared to the corresponding period of fiscal 2014. The decrease in general and administrative expenses was primarily due to \$0.4 million of personnel costs, \$0.4 million of travel costs and \$0.3 million of professional service fees.

General and administrative expenses increased by \$1.8 million or 6.1% for the nine months ended March 31, 2015, as compared to the corresponding periods of fiscal 2014. The increase in general and administrative expenses was primarily due to \$2.8 million in higher personnel costs, \$0.9 million for professional services fees and \$0.5 million for recruiting fees due to an increase in headcount of approximately 100 employees, higher occupancy costs due to additional facilities in Salem, New Hampshire and Shannon, Ireland as a result of our acquisition of Enterasys and a \$1.0 million increase in bad debt expense. This increase was partial offset by \$0.6 million in lower travel costs.

### Acquisition and Integration Costs

Acquisition and Integration costs include those expenses that the company has incurred as result of the acquisition of Enterasys and the related subsequent integration of the two companies. The Company expects to continue to incur integration costs for the remainder of fiscal 2015.

We incurred \$1.7 million and \$9.3 million of integration costs during the three and nine months ended March 31, 2015, respectively primarily for IT, warehouse, and sales integration and severance costs. The Company incurred \$6.4 million and \$18.8 million of acquisition and integration costs during the three and nine months ended March 31, 2014, respectively.

### Amortization of Intangibles

During the three and nine months ended March 31, 2015, we recorded \$4.5 million and \$13.4 million, respectively of amortization expense and during the three and nine months ended March 31, 2014, we recorded \$7.7 million and



\$11.4 million, respectively, of amortization expense, primarily for certain intangible assets related to our acquisition of Enterasys.

Table of Contents

## Interest Expense

Interest expense is comprised of interest charges related to the Credit Facility we entered into on October 31, 2013. We recorded interest expense of \$0.8 million in each of the three months ended March 31, 2015 and 2014. We recorded interest expense of \$2.4 million and \$1.3 million during the nine months ended March 31, 2015 and 2014, respectively.

## Other Expense, Net

Other expense, net increased by \$0.4 million in the third quarter of fiscal 2015, compared to the corresponding period of fiscal 2014. The increase in other expense, net was primarily due to gains from the revaluation of certain assets and liabilities denominated in foreign currencies into U.S. Dollars.

Other expense, net decreased by \$0.3 million in the nine months ended March 31, 2015, compared to the corresponding period of fiscal 2014. The decrease in other expense, net was primarily due to losses from the revaluation of certain assets and liabilities denominated in foreign currencies into U.S. Dollars.

## Provision for Income Taxes

For the three and nine months ended March 31, 2015, we recorded an income tax provision of \$1.1 million and \$3.5 million, respectively. For the three and nine months ended March 31, 2014, we recorded an income tax provision of \$0.9 million and \$2.3 million, respectively.

The income tax provisions for the three and nine months ended March 31, 2015 and 2014, consisted primarily of taxes on the income of our foreign subsidiaries as well as tax expense associated with the establishment of a U.S. deferred tax liability for amortizable goodwill resulting from the acquisition of Enterasys.

## Item 3. Quantitative and Qualitative Disclosures About Market Risk

## Interest Rate Sensitivity

## Investments

The primary objective of our investment activities is to preserve principal while at the same time maximize the income we receive from our investments without significantly increasing risk. Some of the securities that we have invested in may be subject to market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline. To minimize this risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, other non-government debt securities and money market funds. The valuation of our investment portfolio is subject to uncertainties that are difficult to predict. Factors that may impact its valuation include changes to credit ratings of the securities, discount rates and ongoing strength and quality of market credit and liquidity.

If the current market conditions deteriorate further, or the anticipated recovery in market values does not occur, we may be required to record impairment charges in future quarters.

The following table presents the amounts of our cash equivalents, short-term investments and marketable securities that are subject to market risk by range of expected maturity and weighted-average interest rates as of March 31, 2015, (in thousands, except percentage):

	Maturing in Three months or less	Three months to one year	Greater than one year	Total	Fair Value
March 31, 2015					
Included in short-term investments	\$21,285	\$—	\$—	\$21,285	\$21,285
Weighted average interest rate	0.07	% —	% —	% 0.07	%

The following tables present hypothetical changes in fair value of the financial instruments held as of March 31, 2015 that are sensitive to changes in interest rates (in thousands):

28

---

Table of Contents

Unrealized gain given a decrease in interest rate of X bps (100 bps)	(50 bps)	Fair value as of March 31, 2015	Unrealized loss given an increase in interest rate of X bps 50 bps	100 bps
\$0	\$0	\$21,285	\$0	\$0

**Debt**

At certain points in time we are exposed to the impact of interest rate fluctuations, primarily in the form of variable rate borrowings from our credit facility.

The following table presents hypothetical changes in interest expense for the quarter ended March 31, 2015, on outstanding credit facility borrowings as of March 31, 2015, that are sensitive to changes in interest rates (in thousands):

Change in interest expense given a decrease in interest rate of X bps* (100 bps)	(50 bps)	Average outstanding debt during the quarter-ended March 31, 2015	Change in interest expense given an increase in interest rate of X bps 50 bps	100 bps
\$(206	) \$(103	) \$82,250	\$103	\$206

**Exchange Rate Sensitivity**

Majority of our sales and expenses are denominated in United States Dollars. While we conduct some sales transactions and incur certain operating expenses in foreign currencies and expect to continue to do so, we do not anticipate that foreign exchange gains or losses will be significant, in part because of our foreign exchange risk management process discussed below.

**Foreign Exchange Forward Contracts**

We record all derivatives on the balance sheet at fair value. Changes in the fair value of derivatives are recognized in earnings as Other expense, net. From time to time, we enter into foreign exchange forward contracts to mitigate the effect of gains and losses generated by the foreign currency forecast transactions related to certain operating expenses and re-measurement of certain assets and liabilities denominated in foreign currencies. These derivatives do not qualify as hedges. As of March 31, 2015, we did not have any forward foreign currency contracts.

Foreign currency transaction gains and losses from operations was a loss of \$0.5 million and \$0.1 million loss for the three months ended March 31, 2015 and 2014, respectively. Foreign currency transaction gains and losses from operations were a \$0.9 million loss and \$1.2 million loss for the nine months ended March 31, 2015 and 2014, respectively.

Table of Contents

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are controls and procedures designed to reasonably assure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934 as amended, such as this Report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and to reasonably assure that such information is accumulated and communicated to our management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), as appropriate to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of our management, including our CEO and CFO, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Report. Based on this evaluation, our CEO and CFO concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Report.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over our financial reporting. There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurances with respect to financial statement preparation. Further because of changes in conditions, the effectiveness of internal control may vary over time.

We assessed the effectiveness of our internal control over financial reporting as of the end of the period covered by this Report. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control-Integrated Framework (1992).

Based on our assessment using those criteria, we concluded that, as of the end of the period covered by this Report, our internal control over financial reporting is effective.

Changes in Internal Control over Financial Reporting

During the nine months ended March 31, 2015, the Company expanded the scope to include the former operations of Enterasys under the assessment of internal controls over financial reporting. There were no other changes in our internal control over financial reporting during the nine months ended March 31, 2015, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Our management, including the CEO and CFO, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Our controls and procedures are designed to provide reasonable assurance that our control system's objective will be met and our CEO and CFO have concluded that our disclosure controls and procedures are effective at the reasonable assurance level. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within Extreme Networks have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events. Projections of any evaluation of the effectiveness of controls in future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Notwithstanding these limitations, our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives. Our CEO and CFO have concluded that our disclosure controls and procedures are, in fact, effective at the

“reasonable assurance” level.

30

---

Table of Contents

PART II. Other Information

Item 1. Legal Proceedings

For information regarding litigation matters that we deem significant, refer to Part I, Item 3, Legal Proceedings of our Annual Report on Form 10-K for the fiscal year ended June 30, 2014 and Note 8 to our Notes to Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report which are incorporated herein by reference.

Item 1A. Risk Factors

The following is a list of risks and uncertainties which may have a material and adverse effect on our business, financial condition or results of operations. The risks and uncertainties set out below are not the only risks and uncertainties we face, and some are endemic to the networking industry.

We cannot assure you that we will be profitable in the future because a number of factors could negatively affect our financial results.

We have a limited history of profitability and have reported losses in some of our prior fiscal years. In addition, in years when we reported profits, we were not profitable in each quarter during those years. We anticipate continuing to incur significant sales and marketing, product development and general and administrative expenses. Any delay in generating or recognizing revenue could result in a loss for a quarter or full year. Even if we are profitable, our operating results may fall below our expectations and those of our investors, which could cause the price of our stock to fall.

We may experience challenges or delays in generating or recognizing revenue for a number of reasons and our revenue and operating results have varied significantly in the past and may vary significantly in the future due to a number of factors, including, but not limited to, the following:

- we are dependent upon obtaining orders during a quarter and shipping those orders in the same quarter to achieve our revenue objectives;
- decreases in the prices of the products that we sell;
- the mix of products sold and the mix of distribution channels through which products are sold;
- acceptance provisions in customer contracts;
- our ability to deliver installation or inspection services by the end of the quarter;
- changes in general and/or specific economic conditions in the networking industry;
- seasonal fluctuations in demand for our products and services;
- a disproportionate percentage of our sales occurring in the last month of the quarter;
- our ability to ship products by the end of a quarter;
- reduced visibility into the implementation cycles for our products and our customers' spending plans;
- our ability to forecast demand for our products, which in the case of lower-than-expected sales, may result in excess or obsolete inventory in addition to non-cancelable purchase commitments for component parts;
- sales to the telecommunications service provider market, which represent a significant source of large product orders, are especially volatile and difficult to forecast;
- product returns or the cancellation or rescheduling of orders;
- announcements and new product introductions by our competitors;
- our ability to develop and support relationships with enterprise customers, service providers and other potential large customers;
- our ability to achieve targeted cost reductions;
- fluctuations in warranty or other service expenses actually incurred;
- our ability to obtain sufficient supplies of sole- or limited-source components for our products on a timely basis;
- increases in the price of the components that we purchase.

Due to the foregoing factors, period-to-period comparisons of our operating results should not be relied upon as an indicator of our future performance.

We may fail to realize the anticipated benefits of the acquisition of Enterasys.

The success of the acquisition of Enterasys Networks Inc., which we acquired on October 31, 2013, will depend on, among other things, our ability to combine the businesses of Extreme and Enterasys in a manner that does not materially disrupt existing relationships and that allows us to achieve anticipated operational synergies. We have faced and will continue to face significant challenges in combining the two operations into one in a timely and efficient manner. The failure to integrate successfully and to manage successfully the challenges presented by the integration process may result in us not achieving the anticipated benefits of the acquisition.



Table of Contents

We have made certain assumptions relating to the acquisition in our forecasts but the actual results could differ materially.

We have made certain assumptions relating to the forecast level of cost savings, synergies and associated costs of the acquisition of Enterasys. Our assumptions relating to the forecast level of cost savings, synergies and associated costs of the acquisition may be inaccurate based on the information available to us, including as the result of the failure to realize the expected benefits of the acquisition, higher than expected transaction and integration costs, including our ability to service new debt, as well as general economic and business conditions that may adversely affect the combined company following the completion of the acquisition.

The global economic environment has and may continue to negatively impact our business and operating results. The challenges and uncertainty currently affecting global economic conditions may negatively impact our business and operating results in the following ways:

- customers may delay or cancel plans to purchase our products and services;
- customers may not be able to pay, or may delay payment of, the amounts that they owe us which may adversely affect our cash flow, the timing of our revenue recognition and the amount of revenue;
- increased pricing pressure may result from our competitors aggressively discounting their products;
- accurate budgeting and planning will be difficult due to low visibility into future sales;
- forecasting customer demand will be more difficult, increasing the risk of either excess and obsolete inventory if our forecast is too high or insufficient inventory to meet customer demand if our forecast is too low; and
- our component suppliers and contract manufacturers have been negatively affected by the economy which may result in product delays and changes in pricing and service levels.

If global economic conditions do not show continued improvement, we believe that we could experience material adverse impacts to our business and operating results.

The combination of our business with the Enterasys' business will continue to require significant management attention, and we expect to incur significant additional integration costs.

The combined company requires us to devote significant management attention and other resources to integrating the two businesses. We may not successfully complete the integration of our operations in a timely manner and may experience disruptions in relationships with customers, suppliers and employees as a result.

Through March 31, 2015, we have incurred transaction and integration costs in connection with the Enterasys acquisition of approximately \$35.0 million. We expect to incur additional costs integrating the companies' operations, product offerings, and personnel, which cannot be estimated accurately at this time. Although we expect that the realization of efficiencies related to the integration of the business will offset incremental transaction, integration and restructuring costs over time, we cannot give any assurance that this net benefit will be achieved. If the total costs of the integration exceed the anticipated benefits of the acquisition, our results of operations could be adversely affected. We expect the average selling prices of our products to decrease, which may reduce gross margin and/or revenue. The network equipment industry has traditionally experienced an erosion of average selling prices due to a number of factors, including competitive pricing pressures, promotional pricing and technological progress. We anticipate that the average selling prices of our products will decrease in the future in response to competitive pricing pressures, excess inventories, increased sales discounts and new product introductions by us or our competitors. We may experience decreases in future operating results due to the erosion of our average selling prices. To maintain our gross margin, we must develop and introduce on a timely basis new products and product enhancements and continually reduce our product costs. Our failure to do so would likely cause our revenue and gross margin to decline. We may engage in future acquisitions that dilute the ownership interests of our stockholders, cause us to incur debt or assume contingent liabilities.

As part of our business strategy, we review acquisition and strategic investment prospects that we believe would complement our current product offerings, augment our market coverage or enhance our technical capabilities, or

otherwise offer growth opportunities. In the event of any future acquisitions, we could:

- issue equity securities which would dilute current stockholders' percentage ownership;
- incur substantial debt;

32

---

Table of Contents

assume contingent liabilities; or  
expend significant cash.

These actions could have a material adverse effect on our operating results or the price of our common stock.

Moreover, even if we do obtain benefits in the form of increased sales and earnings, these benefits may be recognized much later than the time when the expenses associated with an acquisition are incurred. This is particularly relevant in cases where it would be necessary to integrate new types of technology into our existing portfolio and new types of products may be targeted for potential customers with which we do not have pre-existing relationships. Acquisitions and investment activities also entail numerous risks, including:

- difficulties in the assimilation of acquired operations, technologies and/or products;
- unanticipated costs associated with the acquisition or investment transaction;
- the diversion of management's attention from other business concerns;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience;
- the potential loss of key employees of acquired organizations; and
- substantial charges for the amortization of certain purchased intangible assets, deferred stock compensation or similar items.

We may not be able to successfully integrate any businesses, products, technologies, or personnel that we might acquire in the future, and our failure to do so could have a material adverse effect on our business, operating results and financial condition.

Our credit facilities impose financial and operating restrictions on us.

Our debt instruments impose, and the terms of any future debt may impose, operating and other restrictions on us.

These restrictions could affect, and in many respects limit or prohibit, among other items, our ability to:

- incur additional indebtedness;
- create liens;
- make investments;
- enter into transactions with affiliates;
- sell assets;
- guarantee indebtedness;
- declare or pay dividends or other distributions to stockholders;
- repurchase equity interests;
- change the nature of our business;
- enter into swap agreements;
- issue or sell capital stock of certain of our subsidiaries; and
- consolidate, merge, or transfer all or substantially all of our assets and the assets of our subsidiaries on a consolidated basis.

The agreements governing our credit facilities also require us to achieve and maintain compliance with specified financial ratios.

A breach of any of these restrictive covenants or the inability to comply with the required financial ratios could result in a default under our debt instruments. If any such default occurs, the lenders under our credit agreement may elect to declare all outstanding borrowings, together with accrued interest and other fees, to be immediately due and payable. The lenders under our credit agreement also have the right in these circumstances to terminate any commitments they have to provide further borrowings. If we are unable to repay outstanding borrowings when due, the lenders under our credit agreement will have the right to proceed against the collateral granted to them to secure the debt. If the debt under our credit agreement were to be accelerated, we cannot give assurance that this collateral would be sufficient to repay our debt.

If we fail to meet our payment or other obligations under our credit agreement, the lenders under such credit agreement could foreclose on, and acquire control of, substantially all of our assets.

Our credit agreement is jointly and severally guaranteed by us and certain of our subsidiaries. Borrowings under our credit facilities are secured by liens on substantially all our assets, including the capital stock of certain of our subsidiaries, and the assets of our subsidiaries that are loan party guarantors. If we are unable to repay outstanding borrowings when due, the lenders under our credit agreement will have the right to proceed against this pledged capital stock and take control of substantially all of our assets.

Table of Contents

We purchase several key components for products from single or limited sources and could lose sales if these suppliers fail to meet our needs.

We currently purchase several key components used in the manufacture of our products from single or limited sources and are dependent upon supply from these sources to meet our needs. Certain components such as tantalum capacitors, SRAM, DRAM, and printed circuit boards, have been in the past, and may in the future be, in short supply. We have encountered, and are likely in the future to encounter, shortages and delays in obtaining these or other components, and this could have a material adverse effect on our ability to meet customer orders. Our principal sole-source components include:

- ASICs;
- Merchant silicon;
- microprocessors;
- programmable integrated circuits;
- selected other integrated circuits;
- custom power supplies; and
- custom-tooled sheet metal.

Our principal limited-source components include:

- flash memory;
- DRAMs and SRAMs;
- printed circuit boards; and
- CAMs
- Connectors
- Timing circuits (crystals & clocks).

We use our forecast of expected demand to determine our material requirements. Lead times for materials and components we order vary significantly, and depend on factors such as the specific supplier, contract terms and demand for a component at a given time. If forecasts exceed orders, we may have excess and/or obsolete inventory, which could have a material adverse effect on our operating results and financial condition. If orders exceed forecasts, we may have inadequate supplies of certain materials and components, which could have a material adverse effect on our ability to meet customer delivery requirements and to recognize revenue.

Generally, we do not have agreements fixing long-term prices or minimum volume requirements from suppliers. From time to time we have experienced shortages and allocations of certain components, resulting in delays in filling orders. Qualifying new suppliers to compensate for such shortages may be time-consuming and costly, and may increase the likelihood of errors in design or production. In addition, during the development of our products, we have experienced delays in the prototyping of our chipsets, which in turn has led to delays in product introductions. Similar delays may occur in the future. Furthermore, the performance of the components as incorporated in our products may not meet the quality requirements of our customers.

Intense competition in the market for networking equipment could prevent us from increasing revenue and maintaining profitability.

The market for network switching solutions is intensely competitive and dominated primarily by Brocade Communications Systems, Inc., Cisco Systems Inc., Dell, Hewlett-Packard Company, Huawei Technologies Co. Ltd., and Juniper Networks, Inc. Most of our competitors have longer operating histories, greater name recognition, larger customer bases, broader product lines and substantially greater financial, technical, sales, marketing and other resources. As a result, these competitors are able to devote greater resources to the development, promotion, sale and support of their products. In addition, they have larger distribution channels, stronger brand names, access to more customers, a larger installed customer base and a greater ability to make attractive offers to channel partners and customers than we do. For example, we have encountered, and expect to continue to encounter, many potential customers who are confident in and committed to the product offerings of our principal competitors. Accordingly, these potential customers may not consider or evaluate our products. When such potential customers have considered

or evaluated our products, we have in the past lost, and expect in the future to lose, sales to some of these customers as large competitors have offered significant price discounts to secure these sales.

The pricing policies of our competitors impact the overall demand for our products and services. Some of our competitors are capable of operating at significant losses for extended periods of time, increasing pricing pressure on our products and services. If we do not maintain competitive pricing, the demand for our products and services, as well as our market share, may decline. From time to time, we may lower the prices of our products and services in response to competitive pressure. When this happens, if we are unable to reduce our component costs or improve operating efficiencies, our revenue and margins will be adversely affected.

Table of Contents

Industry consolidation may lead to stronger competition and may harm our operating results.

There has been a trend toward industry consolidation in our markets for several years. We expect this trend to continue as companies attempt to strengthen or hold their market positions in an evolving industry and as companies are acquired or are unable to continue operations. For example, some of our current and potential competitors for enterprise data center business have made acquisitions, or announced new strategic alliances, designed to position them with the ability to provide end-to-end technology solutions for the enterprise data center. Companies that are strategic alliance partners in some areas of our business may acquire or form alliances with our competitors, thereby reducing their business with us. We believe that industry consolidation may result in stronger competitors that are better able to compete as sole-source vendors for customers. This could lead to more variability in our operating results and could have a material adverse effect on our business, operating results, and financial condition.

Furthermore, particularly in the service provider market, rapid consolidation will lead to fewer customers, with the effect that loss of a major customer could have a material impact on results not anticipated in a customer marketplace composed of more numerous participants.

We intend to invest in engineering, sales, service, marketing and manufacturing on a long term basis, and delays or inability to attain the expected benefits may result in unfavorable operating results.

While we intend to focus on managing our costs and expenses, over the long term, we also intend to invest in personnel and other resources related to our engineering, sales, service, marketing and manufacturing functions as we focus on our foundational priorities, such as leadership in our core products and solutions and architectures for business transformation. We are likely to recognize the costs associated with these investments earlier than some of the anticipated benefits and the return on these investments may be lower, or may develop more slowly, than we expect. If we do not achieve the benefits anticipated from these investments, or if the achievement of these benefits is delayed, our operating results may be adversely affected.

Our success is dependent on our ability to continually introduce new products and features that achieve broad market acceptance.

The network equipment market is characterized by rapid technological progress, frequent new product introductions, changes in customer requirements and evolving industry standards. If we do not regularly introduce new products in this dynamic environment, our product lines will become obsolete. These new products must be compatible and inter-operate with products and architectures offered by other vendors. We have and may in the future experience delays in product development and releases, and such delays have and could in the future adversely affect our ability to compete and our operating results.

When we announce new products or product enhancements or end of sale existing products that have the potential to replace or shorten the life cycle of our existing products, customers may defer or cancel orders for our existing products. These actions could have a material adverse effect on our operating results by unexpectedly decreasing sales, increasing inventory levels of older products and exposing us to greater risk of product obsolescence.

Even if we introduce new switching products, alternative technologies could achieve widespread market acceptance and displace the Ethernet technology on which we have based our product architecture. For example, developments in routers and routing software could significantly reduce demand for our products. As a result, we may not be able to achieve widespread market acceptance of our current or future products.

If we do not successfully anticipate technological shifts, market needs and opportunities, and develop products and product enhancements that meet those technological shifts, needs and opportunities, or if those products are not made available in a timely manner or do not gain market acceptance, we may not be able to compete effectively and our ability to generate revenues will suffer.

We cannot guarantee that we will be able to anticipate future technological shifts, market needs and opportunities or be able to develop new products or product enhancements to meet such technological shifts, needs or opportunities in a timely manner or at all. For example, the move from traditional network infrastructures towards SDN has been receiving considerable attention. In our view, it will take several years to see the full impact of SDN, and we believe the successful products and solutions in this market will combine hardware and software elements together. If we fail

to anticipate market requirements or fail to develop and introduce new products or product enhancements to meet those needs in a timely manner, it could cause us to lose customers, and such failure could substantially decrease or delay market acceptance and sales of our present and future products, which would significantly harm our business, financial condition, and results of operations. Even if we are able to anticipate, develop, and commercially introduce new products and enhancements, there can be no assurance that new products or enhancements will achieve widespread market acceptance.



Table of Contents

Claims of infringement by others may increase and the resolution of such claims may adversely affect our operating results.

Our industry is characterized by the existence of a large number of patents and frequent claims and related litigation regarding patents, copyrights (including rights to “open source” software), and other intellectual property rights. Because of the existence of a large number of patents in the networking field, the secrecy of some pending patents and the issuance of new patents at a rapid pace, it is not possible to determine in advance if a product or component might infringe the patent rights of others. Because of the potential for courts awarding substantial damages, the lack of predictability of such awards, and the high legal costs associated with the defense of such patent infringement matters that would be expended to prove lack of infringement, it is not uncommon for companies in our industry to settle even potentially unmeritorious claims for very substantial amounts. Further, the entities with whom we have or could have disputes or discussions include entities with extensive patent portfolios and substantial financial assets. These entities are actively engaged in programs to generate substantial revenue from their patent portfolios and are seeking or may seek significant payments or royalties from us and others in our industry.

Litigation resulting from claims that we are infringing the proprietary rights of others has resulted and could in the future result in substantial costs and a diversion of resources, and could have a material adverse effect on our business, financial condition and results of operations. We have received notices from entities alleging that we may be infringing their patents, and we are currently parties to patent litigation as described under Part I, Item 3, Legal Proceedings. Without regard to the merits of these or any other claims, an adverse court order or a settlement could require us, among other actions, to:

- stop selling our products that incorporate the challenged intellectual property;
- obtain a royalty bearing license to sell or use the relevant technology, and that license may not be available on reasonable terms or available at all;
- pay damages; or
- redesign those products that use the disputed technology.

In addition, our products include so-called “open source” software. Open source software is typically licensed for use at no initial charge, but imposes on the user of the open source software certain requirements to license to others both the open source software as well as modifications to the open source software under certain circumstances. Our use of open source software subjects us to certain additional risks for the following reasons:

- open source license terms may be ambiguous and may result in unanticipated obligations regarding the licensing of our products and intellectual property;
- open source software cannot be protected under trade secret law;
- suppliers of open-source software do not provide the warranty, support and liability protections typically provided by vendors who offer proprietary software; and
- it may be difficult for us to accurately determine the developers of the open source code and whether the acquired software infringes third-party intellectual property rights.

We believe that even if we do not infringe the rights of others, we will incur significant expenses in the future due to defense of legal claims, disputes or licensing negotiations, though the amounts cannot be determined. These expenses may be material or otherwise adversely affect our operating results.

Our operating results may be negatively affected by defending or pursuing claims or lawsuits.

We have and may in the future pursue or be subject to claims or lawsuits in the normal course of our business. In addition to the intellectual property lawsuits described above, we are currently parties to other litigation as described in Part I, Item 3. Legal Proceedings. Regardless of the result, litigation can be expensive, lengthy and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. An unfavorable resolution of a lawsuit in which we are a defendant could result in a court order against us or payments to other parties that would have an adverse effect on our business, results of operations, or financial condition. Even if we are successful in prosecuting claims and lawsuits, we may not recover damages sufficient to cover our expenses incurred to manage, investigate and pursue the litigation. In addition, subject to certain limitations, we may be obligated to indemnify our current and former directors, officers and employees in certain lawsuits. We do not maintain adequate insurance coverage to cover all of our litigation costs and liabilities.

If we fail to protect our intellectual property, our business could suffer.

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. However, we cannot ensure that the actions we have taken will adequately protect our intellectual property rights or that other parties will not independently develop similar or competing products that do not infringe on our patents. We generally enter into confidentiality, invention assignment or license agreements with our employees, consultants and other third parties with whom we do business, and control access to and distribution of our intellectual property and other proprietary information. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise misappropriate or use our products or technology, which would adversely affect our business.

Table of Contents

When our products contain undetected errors, we may incur significant unexpected expenses and could lose sales. Network products frequently contain undetected errors when new products or new versions or updates of existing products are released to the marketplace. In the past, we have experienced such errors in connection with new products and product updates. We have experienced component problems in prior years that caused us to incur higher than expected warranty, service costs and expenses, and other related operating expenses. In the future, we expect that, from time to time, such errors or component failures will be found in new or existing products after the commencement of commercial shipments. These problems may have a material adverse effect on our business by causing us to incur significant warranty, repair and replacement costs, diverting the attention of our engineering personnel from new product development efforts, delaying the recognition of revenue and causing significant customer relations problems. Further, if products are not accepted by customers due to such defects, and such returns exceed the amount we accrued for defective returns based on our historical experience, our operating results would be adversely affected.

Our products must successfully interoperate with products from other vendors. As a result, when problems occur in a network, it may be difficult to identify the sources of these problems. The occurrence of system errors, whether or not caused by our products, could result in the delay or loss of market acceptance of our products and any necessary revisions may cause us to incur significant expenses. The occurrence of any such problems would likely have a material adverse effect on our business, operating results and financial condition.

Our dependence on an OEM for a portion of our wireless products could harm our operating results.

We historically relied exclusively on Motorola for our wireless product offering. With the integration of Extreme Networks with Enterasys Networks, we have two lines of wireless products. We have issued our last purchase order for manufacturing for the line of wireless products manufactured by Motorola. However, we will continue to rely on Motorola for several years for hardware and software support for projected new sales and our existing customer base. Should Motorola cease to timely or effectively honor these supply and support obligations, it may create financial liabilities for us that could have a material adverse effect on our business and operating results.

Our dependence on few manufacturers for our manufacturing requirements could harm our operating results.

We primarily rely on our manufacturing partners; Alpha Networks, Inc. headquartered in Hsinchu, Taiwan, Flextronics, Inc. headquartered in Singapore, and select other partners to manufacture our products. We have experienced delays in product shipments from our manufacturing partners in the past, which in turn delayed product shipments to our customers. These or similar problems may arise in the future, such as delivery of products of inferior quality, delivery of insufficient quantity of products, or the interruption or discontinuance of operations of a manufacturer, any of which could have a material adverse effect on our business and operating results. In addition, any natural disaster or business interruption to our manufacturing partners could significantly disrupt our business. While we maintain strong relationships with our manufacturing partners, our agreements with these manufacturers are generally of limited duration and pricing, quality and volume commitments are negotiated on a recurring basis. The failure to maintain continuing agreements with our manufacturing partners could adversely affect our business. We intend to introduce new products and product enhancements, which will require that we rapidly achieve volume production by coordinating our efforts with those of our suppliers and contract manufacturers.

As part of our cost-reduction efforts, we will need to realize lower per unit product costs from our manufacturing partner by means of volume efficiencies and the utilization of manufacturing sites in lower-cost geographies. However, we cannot be certain when or if such price reductions will occur. The failure to obtain such price reductions would adversely affect our operating results.

Regulations related to disclosure requirements regarding conflict minerals may force us to incur additional compliance expenses and make our supply chain more complex.

On August 22, 2012, as mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the SEC adopted new disclosure regulations for public companies that manufacture products that contain certain minerals and their derivatives, namely tin, tantalum, tungsten or gold, known as conflict minerals, if these minerals are necessary to the functionality or production of the company's products. These regulations require issuers to report annually whether or not such minerals originate from the Democratic Republic of Congo ("DRC") and adjoining

countries and in some cases to perform extensive due diligence on their supply chains for such minerals. The implementation of these new requirements could adversely affect the sourcing, availability and pricing of conflict minerals used in the manufacture of networking equipment, including our products. In addition, we may incur additional costs to comply with the disclosure requirements, including costs related to determining the source of any of the relevant minerals used in our products. Since our supply chain is complex, the due diligence procedures that we implement may not enable us to ascertain the origins for these minerals or determine that these minerals are DRC conflict free, which may harm our reputation. We may also face difficulties in satisfying customers who may require that our products be certified as DRC conflict free, which could harm our relationships with these customers and lead to a loss of revenue. These new requirements also

Table of Contents

could have the effect of limiting the pool of suppliers from which we source these minerals, and we may be unable to obtain conflict-free minerals at competitive prices, which could increase our costs and adversely affect our manufacturing operations and our profitability.

We depend upon international sales for a significant portion of our revenue which imposes a number of risks on our business.

International sales constitute a significant portion of our net revenue. Our ability to grow will depend in part on the expansion of international sales. Our international sales primarily depend on the success of our resellers and distributors. The failure of these resellers and distributors to sell our products internationally would limit our ability to sustain and grow our revenue. There are a number of risks arising from our international business, including:

- longer accounts receivable collection cycles;
- difficulties in managing operations across disparate geographic areas;
- difficulties associated with enforcing agreements through foreign legal systems;
- higher credit risks requiring cash in advance or letters of credit;
- difficulties in safeguarding intellectual property;
- political and economic turbulence;
- terrorism, war or other armed conflict;
- natural disasters and epidemics;
- potential adverse tax consequences;
- compliance with regulatory requirements of foreign countries, including compliance with rapidly evolving environmental regulations;
- compliance with U.S. laws and regulations pertaining to the sale and distribution of products to customers in foreign countries, including export controls and anti-corruption laws, including the Foreign Corrupt Practices Act; and
- the payment of operating expenses in local currencies, which exposes us to risks of currency fluctuations.

Our international sales are primarily U.S. dollar-denominated. Future increases in the value of the U.S. dollar relative to foreign currencies could make our products less competitive in international markets. We invoice some of our international customers in local currency, which would expose us to fluctuations in exchange rates between the U.S. dollar and the particular local currency. If we do so, we may decide to engage in hedging transactions to minimize the risk of such fluctuations.

We have entered into foreign exchange forward contracts to offset the impact of payment of operating expenses in local currencies to some of our operating foreign subsidiaries. However, if we are not successful in managing these foreign currency transactions, we could incur losses from these activities.

We must continue to develop and increase the productivity of our indirect distribution channels to increase net revenue and improve our operating results.

Our distribution strategy focuses primarily on developing and increasing the productivity of our indirect distribution channels. If we fail to develop and cultivate relationships with significant channel partners, or if these channel partners are not successful in their sales efforts, sales of our products may decrease and our operating results could suffer.

Many of our channel partners also sell products from other vendors that compete with our products. Our channel partners may not continue to market or sell our products effectively or to devote the resources necessary to provide us with effective sales, marketing and technical support. We may not be able to successfully manage our sales channels or enter into additional reseller and/or distribution agreements. Our failure to do any of these could limit our ability to grow or sustain revenue.

Our operating results for any given period have and will continue to depend to a significant extent on large orders from a relatively small number of channel partners and other customers. However, we do not have binding purchase commitments from any of them. A substantial reduction or delay in sales of our products to a significant reseller, distributor or other customer could harm our business, operating results and financial condition because our expense levels are based on our expectations as to future revenue and to a large extent are fixed in the short term. Under specified conditions, some third-party distributors are allowed to return products to us and unexpected returns could adversely affect our results.

The sales cycle for our products is long and we may incur substantial non-recoverable expenses or devote significant resources to sales that do not occur when anticipated.

Our products represent a significant strategic decision by a customer regarding its communications infrastructure. The decision by customers to purchase our products is often based on the results of a variety of internal procedures associated with the evaluation, testing, implementation and acceptance of new technologies. Accordingly, the product evaluation process frequently results in a lengthy sales cycle, typically ranging from three months to longer than a year, and as a result, our ability to sell products is subject to a number of significant risks, including risks that:

Table of Contents

budgetary constraints and internal acceptance reviews by customers will result in the loss of potential sales; there may be substantial variation in the length of the sales cycle from customer to customer, making decisions on the expenditure of resources difficult to assess; we may incur substantial sales and marketing expenses and expend significant management time in an attempt to initiate or increase the sale of products to customers, but not succeed; if a sales forecast from a specific customer for a particular quarter is not achieved in that quarter, we may be unable to compensate for the shortfall, which could harm our operating results; and downward pricing pressures could occur during the lengthy sales cycle for our products.

Accordingly, our financial performance in a specific quarter is both difficult to forecast and subject to volatility. Any failure to achieve expected revenues, gross margin or net earnings per share could materially and adversely impact the value of our stock, our future financial prospects and employee retention which is based in part on the perceived value of equity compensation.

Our revenues may decline as a result of changes in public funding of educational institutions.

A portion of our revenues comes from sales to both public and private K-12 educational institutions. Public schools receive funding from local tax revenue, and from state and federal governments through a variety of programs, many of which seek to assist schools located in underprivileged or rural areas. The funding for a portion of our sales to U.S. K-12 educational institutions comes from a federal funding program known as the E-Rate program. E-Rate is a program of the Federal Communications Commission that subsidizes the purchase of approved telecommunications, Internet access, and internal connection costs for eligible public educational institutions. The E-Rate program, its eligibility criteria, the timing and specific amount of federal funding actually available and which Wi-Fi infrastructure and product sectors will benefit, are uncertain and subject to final federal program approval and funding appropriation continues to be under review by the Federal Communications Commission and there can be no assurance that this program or its equivalent will continue, and as a result, our business may be harmed. Furthermore, if state or local funding of public education is significantly reduced because of legislative or policy changes or by reductions in tax revenues due to changing economic conditions, our sales to educational institutions may be negatively impacted by these changed conditions. Any reduction in spending on information technology systems by educational institutions would likely materially and adversely affect our business and results of operations. This is a specific example of the many factors which add additional uncertainty to our future revenue from our education end-customers.

To successfully manage our business or achieve our goals, we must attract, retain, train, motivate, develop and promote key employees, and failure to do so can harm us.

Our success depends to a significant degree upon the continued contributions of our key management, engineering, sales and marketing, service and operations personnel, many of whom would be difficult to replace. We do not have employment contracts with these individuals that mandate that they render services for any specific term, nor do we carry life insurance on any of our key personnel. We have experienced and may in the future experience significant turnover in our executive personnel. In addition, retention has generally become more difficult for us, in part because the exercise price of most of the stock options granted to many of our employees is above the market price. As a result, we experienced high levels of attrition. We believe our future success will also depend in large part upon our ability to attract and retain highly skilled managerial, engineering, sales and marketing, service, finance and operations personnel. The market for these personnel is competitive, and we have had difficulty in hiring employees, particularly engineers, in the time-frame we desire.

Companies in the networking industry whose employees accept positions with competitors frequently claim that competitors have engaged in unfair hiring practices. We have from time to time been involved in claims like this with other companies and, although to date they have not resulted in material litigation, we do not know whether we will be involved in additional claims in the future. We could incur substantial costs in litigating any such claims, regardless of

the merits.

Failure to successfully expand our sales and support teams or educate them in regard to technologies and our product families may harm our operating results.

The sale of our products and services requires a concerted effort that is frequently targeted at several levels within a prospective customer's organization. We may not be able to increase net revenue unless we expand our sales and support teams in order to address all of the customer requirements necessary to sell our products.

We cannot assure you that we will be able to successfully integrate employees into our company or to educate and train current and future employees in regard to rapidly evolving technologies and our product families. A failure to do so may hurt our revenue growth and operating results.

39

---



Table of Contents

Failure of our products to comply with evolving industry standards and complex government regulations may adversely impact our business.

If we do not comply with existing or evolving industry standards and government regulations, we may not be able to sell our products where these standards or regulations apply. The network equipment industry in which we compete is characterized by rapid changes in technology and customers' requirements and evolving industry standards. As a result, our success depends on:

- the timely adoption and market acceptance of industry standards, and timely resolution of conflicting U.S. and international industry standards; and

- our ability to influence the development of emerging industry standards and to introduce new and enhanced products that are compatible with such standards.

In the past, we have introduced new products that were not compatible with certain technological standards, and in the future, we may not be able to effectively address the compatibility and interoperability issues that arise as a result of technological changes and evolving industry standards.

Our products must also comply with various U.S. federal government regulations and standards defined by agencies such as the Federal Communications Commission, standards established by governmental authorities in various foreign countries and recommendations of the International Telecommunication Union. In some circumstances, we must obtain regulatory approvals or certificates of compliance before we can offer or distribute our products in certain jurisdictions or to certain customers. Complying with new regulations or obtaining certifications can be costly and disruptive to our business.

If we do not comply with existing or evolving industry standards or government regulations, we will not be able to sell our products where these standards or regulations apply, which may prevent us from sustaining our net revenue or achieving profitability.

If we do not adequately manage and evolve our financial reporting and managerial systems and processes, our ability to manage and grow our business may be harmed.

Our ability to successfully implement our business plan and comply with regulations requires an effective planning and management process. We need to continue improving our existing, and implement new, operational and financial systems, procedures and controls. We need to ensure that the businesses acquired are appropriately integrated in our financial systems. We integrated the financial and other key managerial systems of Enterasys with Extreme effective July 1, 2014, the first day of our fiscal 2015. Any delay in the implementation of, or disruption in the integration of acquired businesses, or delay and disruption in the transition to, new or enhanced systems, procedures or controls, could harm our ability to record and report financial and management information on a timely and accurate basis, or to forecast future results.

Changes in the effective tax rate including from the release of the valuation allowance recorded against our net U.S. deferred tax assets, or adverse outcomes resulting from examination of our income or other tax returns or change in ownership, could adversely affect our results.

Our future effective tax rates may be volatile or adversely affected by changes in our business or U.S. or foreign tax laws, including: the partial or full release of the valuation allowance recorded against our net U.S. deferred tax assets; expiration of or lapses in the research and development tax credit laws; transfer pricing adjustments; tax effects of stock-based compensation; or costs related to restructurings. In addition, we are subject to the examination of our income tax returns by the Internal Revenue Service and other tax authorities. Although we regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes, there is no assurance that such determinations by us are in fact adequate. Changes in our effective tax rates or amounts assessed upon examination of our tax returns may have a material, adverse impact on our cash flows and our financial condition.

Our future effective tax rate in particular could be adversely affected by a change in ownership pursuant to U.S. Internal Revenue Code Section 382. If a change in ownership occurs, it may limit our ability to utilize our net operating losses to offset our U.S. taxable income. If U.S. taxable income is greater than the change in ownership limitation, we will pay a higher rate of tax with respect to the amount of taxable income that exceeds the limitation. This could have a material adverse impact on our results of operations. On April 26, 2012, we adopted an

Amended and Restated Rights Agreement to help protect our assets (the “Rights Agreement”). In general, this does not allow a stockholder to acquire more than 4.95% of our outstanding common stock without a waiver from our board of directors, who must take into account the relevant tax analysis relating to potential limitation of our net operating losses. The Rights Agreement was ratified by majority of stockholders at the 2014 annual meeting of the stockholder and is effective through May 31, 2015.

Table of Contents

Compliance with laws, rules and regulations relating to corporate governance and public disclosure may result in additional expenses.

Federal securities laws, rules and regulations, as well as NASDAQ Stock Market rules and regulations, require companies to maintain extensive corporate governance measures, impose comprehensive reporting and disclosure requirements, set strict independence and financial expertise standards for audit and other committee members and impose civil and criminal penalties for companies and their Chief Executive Officers, Chief Financial Officers and directors for securities law violations. These laws, rules and regulations and the interpretation of these requirements are evolving, and we are making investments to evaluate current practices and to continue to achieve compliance, which investments may have a material impact on the Company's financial condition.

Our headquarters and some significant supporting businesses are located in northern California and other areas subject to natural disasters that could disrupt our operations and harm our business.

Our corporate headquarters are located in Silicon Valley in Northern California. Historically, this region as well as our R&D centers in North Carolina and New Hampshire have been vulnerable to natural disasters and other risks, such as earthquakes, fires, floods and tropical storms, which at times have disrupted the local economy and posed physical risks to our property. We have contract manufacturers located in Taiwan where similar natural disasters and other risks may disrupt the local economy and pose physical risks to our property and the property of our contract manufacturer.

In addition, the continued threat of terrorism and heightened security and military action in response to this threat, or any future acts of terrorism, may cause further disruptions to the economies of the U.S. and other countries. If such disruptions result in delays or cancellations of customer orders for our products, our business and operating results will suffer.

We currently do not have redundant, multiple site capacity in the event of a natural disaster, terrorist act or other catastrophic event. In the event of such an occurrence, our business would suffer.

Our stock price has been volatile in the past and our stock price may significantly fluctuate in the future.

In the past, our common stock price has fluctuated significantly. This could continue as we or our competitors announce new products, our results or those of our customers or competition fluctuate, conditions in the networking or semiconductor industry change, or when investors, change their sentiment toward stocks in the networking technology sector.

In addition, fluctuations in our stock price and our price-to-earnings multiple may make our stock attractive to momentum, hedge or day-trading investors who often shift funds into and out of stock rapidly, exacerbating price fluctuations in either direction, particularly when viewed on a quarterly basis.

Provisions in our charter documents and Delaware law and our adoption of a stockholder rights plan may delay or prevent an acquisition of Extreme, which could decrease the value of our Common Stock.

Our certificate of incorporation and bylaws and Delaware law contain provisions that could make it more difficult for a third party to acquire us without the consent of our Board of Directors. Delaware law also imposes some restrictions on mergers and other business combinations between us and any holder of 15% or more of our outstanding common stock. In addition, our Board of Directors has the right to issue preferred stock without stockholder approval, which could be used to dilute the stock ownership of a potential hostile acquirer. Although we believe these provisions of our certificate of incorporation and bylaws and Delaware law will provide for an opportunity to receive a higher bid by requiring potential acquirers to negotiate with our Board of Directors, these provisions apply even if the offer may be considered beneficial by some of our stockholders.

Our Rights Agreement provides that if a single stockholder (or group) acquires more than 4.95% of our outstanding common stock without a waiver from our Board of Directors, each holder of one share of our common stock (other than the stockholder or group who acquired in excess of 4.95% of our common stock) may purchase a fractional share of our preferred stock that would result in substantial dilution to the triggering stockholder or group. Accordingly, although this plan is designed to prevent any limitation on the utilization of our net operating losses by avoiding issues raised under Section 382 of the U.S. Internal Revenue Code, the Rights Agreement could also serve as a deterrent to stockholders wishing to effect a change of control.

We rely on the availability of third-party licenses

Some of our products are designed to include software or other intellectual property, including open source software, licensed from third parties. It may be necessary in the future to seek or renew licenses relating to various aspects of these products. There can be no assurance that the necessary licenses would be available on acceptable terms, if at all. The inability to obtain certain licenses or other rights or to obtain such licenses or rights on favorable terms, or the need to engage in litigation regarding these matters, could have a material adverse effect on our business, operating results, and financial condition. Moreover, the inclusion in our products of software or other intellectual property licensed from third parties on a nonexclusive basis could limit our ability

41

---

Table of Contents

to protect our proprietary rights in our products. Further, the failure to comply with the terms of any license, including free open source software, may result in our inability to continue to use such license. Our inability to maintain or re-license any third-party licenses required in our products or our inability to obtain third-party licenses necessary to develop new products and product enhancements, could require us, if possible, to develop substitute technology or obtain substitute technology of lower quality or performance standards or at a greater cost, any of which could delay or prevent product shipment and harm our business, financial condition, and results of operations.

System security risks, data protection breaches, and cyber-attacks could compromise our proprietary information, disrupt our internal operations and harm public perception of our products, which could adversely affect our business. In the ordinary course of business, we store sensitive data, including intellectual property, our proprietary business information and that of our customers, suppliers and business partners on our networks. The secure maintenance of this information is critical to our operations and business strategy. Increasingly, companies, including Extreme Networks, are subject to a wide variety of attacks on their networks on an ongoing basis. Despite our security measures, Extreme Networks' information technology and infrastructure may be vulnerable to penetration or attacks by computer programmers and hackers, or breached due to employee error, malfeasance or other disruptions. Any such breach could compromise our networks, creating system disruptions or slowdowns and exploiting security vulnerabilities of our products, and the information stored on our networks could be accessed, publicly disclosed, lost or stolen, which could subject us to liability to our customers, suppliers, business partners and others, and cause us reputational and financial harm. In addition, sophisticated hardware and operating system software and applications that we produce or procure from third parties may contain defects in design or manufacture, including "bugs" and other problems that could unexpectedly interfere with the operation of our networks.

If an actual or perceived breach of network security occurs in our network or in the network of a customer of our networking products, regardless of whether the breach is attributable to our products, the market perception of the effectiveness of our products could be harmed. In addition, the economic costs to us to eliminate or alleviate cyber or other security problems, bugs, viruses, worms, malicious software systems and security vulnerabilities could be significant and may be difficult to anticipate or measure. Because the techniques used by computer programmers and hackers, many of whom are highly sophisticated and well-funded, to access or sabotage networks change frequently and generally are not recognized until after they are used, we may be unable to anticipate or immediately detect these techniques. This could impede our sales, manufacturing, distribution or other critical functions, which could adversely affect our business.

Market conditions and changes in the industry could lead to discontinuation of our products or businesses resulting in asset impairments

In response to changes in industry and market conditions, we may be required to strategically realign our resources and consider restructuring, disposing of, or otherwise exiting businesses. Any decision to limit investment in or dispose of or otherwise exit businesses may result in the recording of special charges, such as inventory and technology-related write-offs, workforce reduction costs, charges relating to consolidation of excess facilities, or claims from third parties who were resellers or users of discontinued products. Our estimates with respect to the useful life or ultimate recoverability of our carrying basis of assets, including purchased intangible assets, could change as a result of such assessments and decisions. Although in certain instances, our supply agreements allow us the option to cancel, reschedule, and adjust our requirements based on our business needs prior to firm orders being placed, our loss contingencies may include liabilities for contracts that we cannot cancel with contract manufacturers and suppliers. Further, our estimates relating to the liabilities for excess facilities are affected by changes in real estate market conditions.

If our products do not effectively inter-operate with our customers' networks and result in cancellations and delays of installations our business could be harmed.

Our products are designed to interface with our customers' existing networks, each of which have different specifications and utilize multiple protocol standards and products from other vendors. Many of our customers' networks contain multiple generations of products that have been added over time as these networks have grown and evolved. Our products must inter-operate with many or all of the products within these networks as well as future

products in order to meet our customers' requirements. If we find errors in the existing software or defects in the hardware used in our customers' networks, we may need to modify our software or hardware to fix or overcome these errors so that our products will inter-operate and scale with the existing software and hardware, which could be costly and could negatively affect our business, financial condition, and results of operations. In addition, if our products do not inter-operate with those of our customers' networks, demand for our products could be adversely affected or orders for our products could be cancelled. This could hurt our operating results, damage our reputation, and seriously harm our business and prospects.

Table of Contents

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

We currently have authority granted by our Board of Directors to repurchase up to \$75.0 million in common stock over a three year period starting October 1, 2012. Since the inception of the program, 4.1 million shares have been repurchased for a total purchase price of \$14.5 million and \$60.5 million of the authorized amount is remaining. We did not repurchase any shares of our common stock for the nine month period ended March 31, 2015.

Item 3. Defaults Upon Senior Securities - Not applicable

Item 4. Mine Safety Disclosure - Not Applicable

Item 5. Other Information

Table of Contents

## Item 6. Exhibits

## (a) Exhibits:

Exhibit Number	Description of Document	Incorporated by Reference			Filed Herewith
		Form	Filing Date	Number	
10.34*	Release of Claims, executed April 29, 2015, between Extreme Networks, Inc. and Charles W. Berger.	8-K	4/29/2015	10.1	
10.35*	Offer Letter, executed April 30, 2015, between Extreme Networks, Inc. and Edward B. Meyercord.	8-K	5/4/2015	10.1	
10.36*	Release of Claims, executed May 1, 2015, between Extreme Networks, Inc. and Edward Carney.	8-K	5/4/2015	10.2	
31.1	Section 302 Certification of Chief Executive Officer				X
31.2	Section 302 Certification of Chief Financial Officer				X
32.1	Section 906 Certification of Chief Executive Officer				X
32.2	Section 906 Certification of Chief Financial Officer				X
101.INS	XBRL Instance Document.				X
101.SCH	XBRL Taxonomy Extension Schema Document.				X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.				X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.				X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.				X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document				X



Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EXTREME NETWORKS, INC.  
(Registrant)

/S/ KENNETH AROLA  
KENNETH AROLA  
Executive Vice President, Chief Financial Officer, and Chief  
Accounting Officer  
May 6, 2015